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Print Edition — September 1st 2001

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Politics this week

Aug 30th 2001
From The Economist print edition

Mustafa Zibri, the 64-year-old leader of the **Popular Front for the Liberation of Palestine** and one of the founders of the Palestinian Liberation Organisation, was assassinated by Israeli forces. Mr Zibri is the most prominent Palestinian to be killed by Israel for more than a decade.

Israeli troops seized Beit Jala, a town in the **West Bank**, in a bid to curb attacks by Palestinian gunmen on Gilo, a Jewish settlement in East Jerusalem. Two days later, both sides agreed to a ceasefire and to withdraw at the same time after pressure from the EU.

See article: The tanks of August

A report by the International Food Policy Research Institute predicted that the number of **malnourished children** around the world would decline slowly over the next 20 years, but would increase by as much as 18% in sub-Saharan Africa.

See article: Feast or famine?

A tax too far

Lionel Jospin, France's prime minister, suggested that the EU take the lead in calling for a global "Tobin tax" on cross-border flows of capital, to reduce currency speculation and volatility. His finance minister, Laurent Fabius, was not amused.

Wim Kok, prime minister of the Netherlands since 1994, announced that he would stand down as leader of the Labour Party, and named his chosen successor to lead it into next May's election: Ad Melkert, now its parliamentary floor leader.

See article: Wim Kok bows (almost) out

In **Macedonia**, a NATO force began collecting weapons surrendered by ethnic-Albanian guerrillas. It said it expected a few thousand; expressing widespread Slav-Macedonian anger, the government said the rebels held vastly more. Germany's Bundestag, with dissent from more than 70 deputies, agreed to back the sending of German troops to join the NATO operation.

See article: Boris Trajkovski

In **Spain**, police struck another big blow against ETA terrorism, arresting most of a "commando unit" in and around Barcelona. ETA hit back with a bomb in the car park of Madrid airport.

With a general election less than a month away, **Poland's** prime minister, Jerzy Buzek, sacked his finance minister, Jaroslaw Bauc, who had recently embarrassed colleagues by predicting that next year's budget deficit could be as big as 11% of GDP.

No asylum

A Norwegian freighter carrying 434 **asylum seekers** rescued from a sinking

Indonesian ferry was refused permission to land them in Australia. The Australian army seized the ship and threatened to sail it out of territorial waters. With the Australian government facing an election soon, it said it was determined to protect the country's "territorial integrity" from would-be immigrants who try to land illegally. Australia takes more than 10,000 refugees a year under a UN scheme.

Afghanistan's ruling **Taliban** allowed Red Cross officials to visit eight imprisoned western aid workers, who will be put on trial accused of the promotion of Christianity in the strictly Muslim country. The aid workers were said to be in good health.

There was a big turnout for **East Timor's** first democratic election after centuries of foreign domination. The Timorese voted for a constituent assembly in a ballot run by the UN. Independence is expected to follow next year.

See article: On the road to independence

China admitted for the first time that it was facing a "very serious" **AIDS** epidemic. The use of unsterilised needles in obtaining blood from donors is believed to have spread the disease.

See article: Confession time

A proposal by **Taiwan** to increase its trade with China to make up for the fall in its exports to the United States was dismissed by the Chinese. Taiwan would first have to accept the principle of "one China", the government said.

See article: Not so strait

China indicated that it plans to relax its **mobility laws**, ending the bureaucracy that bars rural people from moving to the cities.

See article: Off to the city

Mexico's energy crisis

The head of **Mexico's** state oil monopoly gave warning that the country's oil exports could drop by two-thirds by 2006 without private investment. The country's president, Vicente Fox, is pushing for tax and energy reforms in a new session of Congress that opens this weekend.

See article: Fox's moment of truth

Seeking to implement an austerity plan aimed at avoiding a debt default, **Argentina's** government said that it plans reforms to health and welfare agencies, as well as a consultative referendum on streamlining the political system.

See article: Culling the politicians

Peru's Congress voted to approve a report accusing Alberto Fujimori, a former president who fled to Japan last year, of crimes against humanity during the war against Maoist terrorists in the early 1990s.

See article: Cleaning up

Colombia's army said that it had killed at least 50 FARC guerrillas and dismantled rebel bases during fighting over the past three weeks.

The Congressional Budget Office announced that **America's budget**, excluding Social Security, will be in deficit by $9 billion in the current financial year. President George Bush's administration had earlier predicted a tiny positive balance. The battle over next year's budget intensified with Mr Bush demanding more money for the armed forces.

See article: Of numbers and a man

Gary Condit appeared on television to half-answer questions about the disappearance of a young intern, Chandra Levy. The beleaguered congressman could be served legal papers contesting his denial of an affair with a flight attendant.

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Business this week

Aug 30th 2001
From The Economist print edition

Plummeting demand for chips claimed yet more victims. **Toshiba**, Japan's biggest chip maker, announced that 19,000 jobs would go, 10% of its worldwide workforce, and that it would drastically cut investment. It also began talks with **Infineon**, a German chip firm, about a merger of their memory-chip operations. **Kyocera**, another chip firm, said it would cut 10,000 jobs, 20% of its workforce.

See article: Lay-offs with no sign of revival

Gateway, an American computer maker, announced that it would shed around 5,000 workers, some 25% of the total, on top of 3,000 job losses announced earlier this year. The job losses follow the company's price war with Dell and declining technology spending as the world economy droops.

Sam Wyly, a wealthy Texan, failed to grab control of the board of **Computer Associates**, the world's fourth-largest software company, after shareholders re-elected all ten incumbents. Mr Wyly had accused the company's management of "chronic abuse of customers and employees" and of letting the share price languish.

AP

AES, a large American power company, made an unsolicited bid worth $1.4 billion to raise its 7% stake and take a controlling interest in **Compania Anonima Nacional Telefonos de Venezuela**, the country's largest telecoms company. A rival bid may come from Spain's Telefonica, which also owns 7% of CANTV.

Lucent Technologies announced the closure of **Chromatis Networks**, an Israeli optical-network equipment maker. The foundering telecoms-equipment giant acquired Chromatis only a year ago for shares valued at $4.5 billion. The same shares are now worth just $590m.

Tyre failure

Firestone was reported to have paid $7.9m to settle a lawsuit for injuries sustained after tyres that it supplied failed on Ford Explorers. Ford had settled before the trial for $6m. The verdict seemed to support Firestone's contention that Ford was partly to blame for the accidents. Firestone may yet face a thousand similar lawsuits.

Poor prospects for the world economy prompted **ThyssenKrupp** to issue a profit warning, its second this year. The German steel firm said third-quarter results had not met expectations and that conditions were unlikely to improve before the end of the year.

The European Commission agreed to allow **Italenergia**, a consortium dominated by Fiat, to take over **Montedison**, Italy's largest private power company. However, the commission said that it would investigate again if Italenergia's junior partner, **Electricité de France**, an acquisitive French power company, were to gain control of Montedison. The commission is also considering the legality of an Italian law that gave EDF, which owns 18% of Italenergia, just 2% of the voting rights.

AP

Volkswagen won agreement from a powerful German trade union, IG Metall, to employ 5,000 extra workers for less pay and with more flexible working arrangements than current employees. The deal came after much

wrangling; representatives of both capital and labour claimed it as a victory.

Cinven, a British venture-capital firm, has reportedly agreed to pay *euro*2 billion ($1.8 billion) to Vivendi, a French media group, for a roster of specialist publications and medical magazines.

Big banks get smaller

Credit Suisse Group, owners of Switzerland's second-biggest bank, announced that profits were down by 23% in the second quarter compared with a year ago, to SFr1.3 billion ($743m). Further cost-cutting at CSFB, its investment- banking arm, was promised; more jobs will probably go on top of the 3,000 departures announced in the past year.

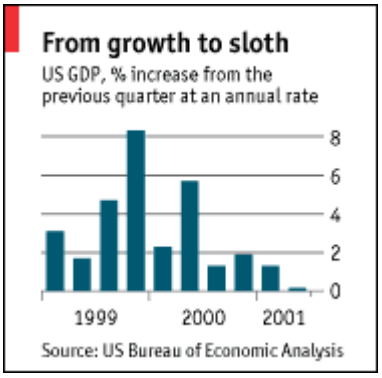
J.P. Morgan Chase joined the list of investment banks feeling the pinch. It said that it planned to cut costs by up to 20%; expect both jobs and bonuses to be cut.

Down at last

The **European Central Bank** cut interest rates by a quarter of a percentage point to 4.25%. Despite widespread and repeated calls to reduce rates, this latest move is only the second cut this year.

See article: The ECB decides

Growth in **America's** GDP for the second quarter was revised down from 0.7% to a paltry 0.2% compared with the previous quarter at an annual rate, the worst performance for eight years. The economy was saved from contracting only by a sharp upward revision of consumer spending, as Americans shopped even though the rest of the economy is sluggish.



See article: Home is where the wealth is

Japan's government reacted to its weakening labour market—its official unemployment rate hit 5% in July—by preparing to unveil measures costing ¥1.7 trillion ($14.2 billion) to assist the jobless. Adding to the gloom, industrial production fell by 2.8% in July, leaving it 8.5% down on a year earlier.

See article: The shadow of joblessness

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Russia's foreign policy

Can Russia handle a changed world?

Aug 30th 2001
From The Economist print edition

Missile-defence talks and NATO enlargement will test Russia's new pragmatism

EVER since the cold war ended, Russia has been searching in vain for a foreign policy worthy of the great power it thinks it still ought to be. From the mutual disappointments of their early bear-hugging "strategic partnership", through Russia's deep sulk over its loss of empire and influence, to the outright hostility that greeted NATO's intervention in Kosovo, western governments too have puzzled over how to manage relations with a country that is too large and well-armed to be overlooked, but all too prickly and unpredictable to be counted on. Vladimir Putin has sensibly tried to counter Russia's drift to the margins of world affairs by presenting himself as a more of a pragmatist to do business with. This autumn, the search for a new strategic understanding with America about nuclear weapons and missile defences, as well as the start of discussions in NATO about further enlargement, will test this new pragmatism to the limit.

If a new rift is to be avoided, by the time Mr Putin meets America's president, George Bush, in November, the two will need to have in their minds, if not yet in detail on paper, the outline of a new strategic bargain that will both dramatically cut their nuclear arsenals and resolve their differences over the future of the Anti-Ballistic Missile (ABM) treaty. Yet success is still far from certain. Part of the difficulty is that it is hard to over-estimate what is at stake in such a deal for Russia.

Mr Putin has been more honest than most in acknowledging that it is not dastardly western plots, but Russia's own economic and political weakness, that has so greatly reduced its standing in the world. By contrast, nuclear weapons and the raft of cold-war-era treaties with America, including the ABM treaty, represent the one flattering measure of Russia's old worth that endures. That is why, although cash-strapped and badly in need of a deal that will cut the numbers of nuclear missiles he needs to maintain, at first Mr Putin simply refused to contemplate tampering with the ABM treaty, which for 30 years has prevented either side from building the sorts of anti-missile defences Mr Bush is now keen to have.

Instead Mr Putin joined China in a chorus of disapproval, and tried to drive an ABM-sharpened wedge between America and its European allies. But the Europeans refused to play along, and common interests with China—which unlike Russia opposes all missile defences, including non-ABM-offending ones, because it worries these may be used someday to protect Taiwan from China—extend only so far. So in June, at his first face-to-face meeting with Mr Bush, Mr Putin at last agreed to explore a new set of strategic understandings with America to replace those of the cold-war years.

Another difficulty, it has to be said, is that America's plans for new defences have barely taken shape. Mr Bush says his aim is to help defend America and its allies against limited new threats from rogue states armed with a few long-range missiles, not from Russia or China. China's deterrent is smaller and therefore potentially more easily undermined by even limited defences, but Russia knows that the sort of defences Mr Bush has talked about, though they would still offend against the ABM treaty as it currently stands, would not threaten Russia. Still, some of Mr Bush's officials talk airily of defences on land, at sea, in the air, even in space. Without some eventual limits on technology, or on numbers of interceptors and how they can be deployed (ruling out weapons in space would help), Mr Putin could have little confidence that the "understandings" with which America says it wants to replace the ABM treaty will protect Russia's interests too.

The best way for Russia to proceed, however, is to negotiate with America in good faith. A Russia ready to think creatively about the elements of a new strategic bargain would also help those on Mr Bush's team who would prefer to have such a stability-preserving deal; there are others, frankly, who would rather press on regardless of Russia. And if the two sides still fail to agree? Russia has no veto over America's defences. America has said it will go ahead unilaterally if no deal is done, and it may yet do just that. But Russia would earn a lot of diplomatic credit for seeking a genuine accord.

Unfortunately, the instinct of Russia's diplomats and generals is still to see the world as a zero-sum game: anything that America wants, or is seen to benefit from, must be bad for Russia. But traditional Russian tactics—turning any negotiation into an endurance test (some of those old arms-control treaties took years to pull off)—will not work with Mr Bush. If Mr Putin really wants talks now under way to get results, he will need to bang heads together on his own side.

It does not help Russia's case that some of its own companies have been doing a lot (alongside China and North Korea) to help would-be proliferators, including Iran, Iraq and Syria, build the bigger missiles that America now sees as a potential new threat. With official approval, Russia's scientists help Iran's nuclear industry, despite the country's barely disguised bid to build a bomb; Russia is also selling nuclear fuel to India, despite that country's refusal of full international safeguards. Rather than opportunistically pocketing the cash from such deals, Mr Putin would do better to stem this flow of technology, which could some day pose a direct threat to Russia too.

Putin-the-pragmatic

Old diplomatic habits die harder in Russia, but when it comes to NATO's further enlargement, Mr Putin may have learned something from past mistakes. When NATO first offered to open its doors to new recruits from Eastern Europe—Poland, Hungary and the Czech Republic—Russia loudly threatened dire consequences, only to discover it had no veto over NATO decisions and had to back down. All its thundering achieved was a lengthening queue of countries mustard-keen to join. At its summit in Prague next year, NATO says it will issue more invitations—how many and for when is yet to be decided. Russia is no keener to see NATO grow, especially as this time the hopefuls include Lithuania, Latvia and Estonia, once part of the old Soviet Union (see article). But so far Mr Putin has kept his cool. There have been dark mutterings that Russia might move its short-range nuclear weapons provocatively closer to NATO territory. But a more pragmatic Russia would instead take a hard look at the damage such cold-war reflexes are already doing to its interests in Europe.

Mr Putin wants Russia to be an accepted European power, but his is still an old-style Europe of spheres of influence and thus he still demands Russia's due in its ex-Soviet parts. Yet the more Russia banks on trouble in places like Georgia in the hope of keeping a grip there, or coddles repressive Belarus, or supports anti-reform elements in Ukraine so as to keep that country economically dependent, the more those countries that can will keep shuffling nervously away from Russia and towards organisations like NATO and the European Union.

Whether Mr Putin likes it or not, Russia has no more of a veto over other Europeans' futures than it does over America's defence. With luck, Putin-the-pragmatist has started to understand that. If he can apply that insight to managing relations with America and with NATO, however tricky, without all the bad-tempered fist-banging of the past, Russia would have the makings of a pragmatic new foreign policy—and show itself to be a worthy power to do business with.

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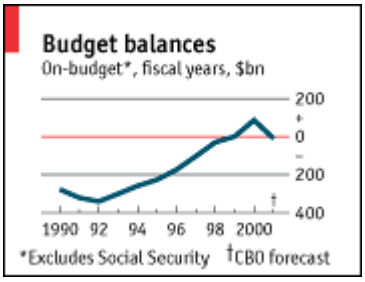
George Bush and the budget

Of numbers and a man

Aug 30th 2001
From The Economist print edition

The president needs to be tough with Congress on spending



NEXT week, Congress reconvenes after the Labour day holiday. September will be dominated by the budget for the next fiscal year, which begins on October 1st. For George Bush, this involves two awkwardnesses. First, Congress, including the newly Democratic Senate, controls the timing of the various spending bills. And second, the whole numbers business has become rather tricky for Mr Bush now that he stands accused of having wasted Bill Clinton's budget surplus on his tax cut. The Congressional Budget Office says that the current year's budget will be balanced only after filching $9 billion from the "untouchable" Social Security trust fund.

Congressional Democrats have reason to think that the budget might win them votes. A recent poll found that Americans are far more likely to hold the president "very responsible" for the declining surplus than them. In fact, Mr Bush should be able to turn the government's finances to his advantage—both in Congress and in the country at large.

Begin with the numbers for the current year. Raiding the pensions of widows to pay off his rich friends certainly ties in with one of Mr Bush's more unfortunate stereotypes. In fact, Mr Bush is more like a robber being charged for burgling one of the few houses he has not visited. The dodgy numbers in Mr Bush's tax cut come not this year, but towards the end of the decade, where he makes heroic assumptions about revenues just when the demands of the retiring baby-boom generation on government services will begin to mount.

This year's tax cut was originally a Democratic idea—and not a bad one at that. A slowing economy demands some fiscal easing. Surpluses tend to be deflationary, because the government takes money out of the economy. Against this background, a deficit of $9 billion in a budget of $2 trillion is close to a neutral position.

As for the Social Security trust fund, dipping into something that you originally promised to use only for paying down the national debt is certainly bad politics. But the trust fund is largely an accounting fiction. What matters far more is, first, pushing ahead with the partial privatisation of the pension system (which would put more money beyond Congress's grasping fingers), and, second, making sure that the government's finances are back in surplus to provide for those baby-boomers.

That means reining in spending programmes—and ties the argument back to Mr Bush's other awkwardness, the battle with Congress over next year's budget. Here the president has already won a victory. For better or worse, his tax cut has changed the tenor of political debate from where to spend the surplus to where to save money. Can Mr Bush reinforce this?

In all there are 13 appropriations bills to pass. Those bills have already earmarked $661 billion of spending. Some analysts calculate that this leaves room for only $9 billion of extra money to be spent without dipping into Social Security. Meanwhile, Mr Bush wants to spend $18 billion more on the armed forces (including $3 billion on missile defences). The House wants to spend even more on education. There are also various demands for more for farmers, more tax breaks and, needless to say, buried within the details, whole piggeries' worth of prime congressional pork for needy constituents.

The Democrats are likely to torment the president: they may well, for instance, keep military spending back till last. As the horse-trading begins, the temptation for Mr Bush will be to bribe his way past his opponents—to agree to their spending plans if they accept his, and to invent some accounting jiggery-

pokery to explain it all. Instead, the accent must be on holding the line (in the final extreme, by use of the veto), reducing his own demands and getting rid of the pork. This has less to do with the current macroeconomic situation, which could easily accommodate and may even require a budget deficit, than his future plans, for which a spending spiral would be lethal. If he can keep spending down now, the rest of his predictions will begin to make more sense.

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Hedge funds

Fool's gold

Aug 30th 2001
From The Economist print edition

They may be becoming boring, but many more people are going to be fleeced by hedge funds

Get article background

IT IS galling. There you are around the barbecue, the only person not smugly invested in hedge funds—which, everybody else is quick to remind you, not only handsomely beat shares during the bull market, but have now kept out of reach of the bears. "Long on equities?", your neighbours sneer, as if you had a bad case of garden gnomes.

Most people can name no more than three hedge funds: Long-Term Capital Management (LTCM), which was bailed out in 1998, and George Soros's Quantum and Julian Robertson's Tiger funds (wound down and closed, respectively, because of their rotten returns). Yet investors are now pouring their money into little-known hedge funds, which have doubled in number over the past five years, to 6,000, managing a total of over $500 billion (see article). They are doing so because they believe that hedge funds always outperform.

One hedge-fund consultant goes further: "You're not buying an asset class, you're buying a skills-set." Hedge funds, that is, are purveyors of alchemy. Take a sample disclosure document. "Buy and sell decisions," it runs, "will, in many cases, be made and executed algorithmically according to quantitative trading strategies embodied in analytical computer software running [the manager's] computer facilities." It is almost like the old spoof of the South Sea bubble era: "an undertaking of great advantage, but no one to know what it is." Who cares that your manager won't tell you how he invests? He's charging you so much (1-2% annual fees, plus 20% of any upside) that he must be good. His $400,000 minimum investment is proof only of his (and your) discrimination. Not for him to be judged by some plebeian benchmark of "relative" performance. He is in the business of "absolute" returns.

For how much longer? Increasingly, institutional investors—notably CalPERS, California's public pension fund, and a group of Ivy League endowments—are investing in hedge funds as a way to spread their risks. Their presence is welcome, for they reject hedge funds' disdain for benchmarking. They want more disclosure about funds' strategies and their risk-management systems. The alchemists' mystique, a key selling-point for rich individuals, is a turn-off for institutional investors, who see it as just one extra, highly idiosyncratic risk.

Hurry, while the fun lasts

In the long run, a flood of institutional money should ensure a less opaque industry, and perhaps also one with fewer chances for spectacular returns. More money will be fighting over the same opportunities: in bond arbitrage, "special situations", distressed debt, and so on. Managing hedge funds will become as boring as managing ordinary ones. Good.

Until then, many more wealthy fools are likely to be parted from their money. Hedge funds are now offered not just to the filthy rich, but to the "mass affluent". The pitch is that hedge funds have produced better, and less volatile, returns than the bond or equity markets as a whole. If that is true—and it is disputed—it is only in the aggregate. Choosing among individual managers and investment styles is near-impossible, given their scant or even misleading information. The term "hedge funds" suggests a judicious balancing of risks, but it is almost always a misnomer. In sympathy for Barbra Streisand, who once lost over 98% of a hedge-fund investment, *The Economist* calls for the industry to be officially renamed. "Goodbye Lolly" funds, perhaps?

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Racism

Don’t discriminate

Aug 30th 2001
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Many groups want governments to discriminate in their favour. But they shouldn’t

Reuters

DURBAN, in South Africa, is a charming city, but delegates attending the UN World Conference Against Racism there this week are too angry to enjoy its beaches or curry houses. America is upset that the draft declaration is too hard on Israel. Western governments are annoyed by demands that they should pay reparations for slavery and colonialism, while many Africans and African-Americans are furious that these demands for reparations have been turned aside. Ethnic groups from all around the world have assembled to trumpet their grievances and demand “remedial measures”.

Most of the Durban delegates, like many race-relations “experts”, tend to agree that bigotry is everywhere, and getting worse. Look at the Balkans, they say, or at America’s inner-city ghettoes. They tend also to argue that most disparities in wealth between different ethnic groups can be blamed on discrimination. Their preferred solutions usually involve governments doing more: not merely forbidding racial discrimination but, when recruiting or awarding contracts, favouring groups which have been victimised. Universities should apply different standards to applicants from such groups. Companies should be obliged to hire and promote more of them.

All this is open to question. Racial discrimination is still a huge problem, and is widely and rightly legislated against. But in many places it appears to be on the wane. In South Africa, a government devoted to keeping whites up and blacks down eventually stood aside peacefully to make way for multi-racial democracy (see article). In Britain, recent race riots obscure the fact that people of different colours for the most part co-exist quite peacefully. Two generations ago, most white Britons probably disapproved of inter-racial marriage. Now, among the young, it is both common and uncontroversial.

As countries have grown richer, so the poorest ethnic groups have benefited too. Sixty years ago in America, 60% of black women with jobs worked as domestic servants. Now, only one in 50 does, and black female college graduates earn more on average than white female graduates. Racist attitudes may still be widespread, but in fewer places do they determine an individual’s life chances. Several ethnic minorities suffer discrimination but are still richer than the majorities among whom they live: the Chinese in South-East Asia, the Indians in east Africa, the Jews in many places.

People from different tribes are not doomed to squabble. Where ethnic antagonism leads to bloodshed, it is usually because politicians have inflamed passions to secure their own grip on power. The tribal wars in ex-Yugoslavia and Rwanda started this way, as did the milder violence in rural Zimbabwe.

Colour-blind is best

The trouble with an emphasis on state activism to combat the problems that do endure is that even well-intentioned governments can do more harm than good. When, for example, the South African government allows black-owned firms to charge more and still win contracts to build houses or lay water-pipes for the poor, this is splendid for blacks who own construction firms, but leaves the poor, who are mainly black, with less shelter or clean water. When American universities admit blacks and Hispanics with lower exam scores than others, they make it more likely that they will fail to graduate at all. In Nigeria, affirmative action in favour of the majority tribes in all 36 states means that, in the words of

Chinua Achebe, a novelist, “It would be difficult to point to one important job held by the most competent person we have.”

It may seem naive to argue that governments should be colour-blind, but wasn’t that Martin Luther King’s dream? All citizens should be equal before the law. States should not discriminate, “positively” or otherwise. There may be sensible exceptions. In countries struggling to end or avoid civil war, or where certain groups have recently been subject to state-mandated discrimination, a short dose of positive discrimination may be the least bad way forward. But such measures should be a last resort, and come with an expiry date.

In most countries, most problems are better tackled without reference to race. Efforts to relieve poverty should focus on poor people. Those who win civil-service jobs through affirmative action tend to be middle-class, and the beneficiaries of “affirmative procurement” are often rich. Likewise in education: if black Americans or native Malays in Malaysia are scoring lower marks than other groups, the answer is to improve their schools, not to tell them they need not meet the same standards as others. Allocating public favours by ethnic group can Balkanise societies and make large chunks of the population reliant on the state. Treating citizens as individuals encourages them to think of themselves that way, and helps break down the stereotypes on which racism thrives.

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Surnames

As easy as ZYX

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From The Economist print edition

It is time to stand up for the alphabetically disadvantaged

OVER the past century, all kinds of unfairness and discrimination have been denounced or made illegal. But one insidious form continues to thrive: alphabetism. This, for those as yet unaware of such a sad affliction, refers to discrimination against those whose surnames begin with a letter in the lower half of the alphabet.

It has long been known that a taxi firm called AAAA cars has a big advantage over Zodiac cars when customers thumb through their phone directories. Less well known is the advantage that Adam Abbott has in life over Zoë Zysman. English names are fairly evenly spread between the halves of the alphabet. Yet a suspiciously large number of top people have surnames beginning with letters between A and K.

Thus the American president and vice-president have surnames starting with B and C respectively; and 26 of George Bush's predecessors (including his father) had surnames in the first half of the alphabet against just 16 in the second half. Even more striking, six of the seven heads of government of the G7 rich countries are alphabetically advantaged (Berlusconi, Blair, Bush, Chirac, Chrétien and Koizumi). The world's three top central bankers (Greenspan, Duisenberg and Hayami) are all close to the top of the alphabet, even if one of them really uses Japanese characters. As are the world's five richest men (Gates, Buffett, Allen, Ellison and Albrecht). To cap it all, the editor, deputy editor and chief executive of *The Economist* are blessed with surnames starting with E, C and A respectively.

Can this merely be coincidence? One theory, dreamt up in all the spare time enjoyed by the alphabetically disadvantaged, is that the rot sets in early. At the start of the first year in infant school, teachers seat pupils alphabetically from the front, to make it easier to remember their names. So short-sighted Zysman junior gets stuck in the back row, and is rarely asked the improving questions posed by those insensitive teachers. At the time the alphabetically disadvantaged may think they have had a lucky escape. Yet the result may be worse qualifications, because they get less individual attention, as well as less confidence in speaking publicly.

The humiliation continues. At university graduation ceremonies, the ABCs proudly get their awards first; by the time they reach the Zysmans most people are literally having a ZZZ. Shortlists for job interviews, election ballot papers, lists of conference speakers and attendees: all tend to be drawn up alphabetically, and their recipients lose interest as they plough through them. Joint authors of economic papers are listed under the name that falls first in the alphabet.

What is to be done? Awkward though it may be for the independent-minded, women can at least achieve alphabetic advancement by marrying "up". Thus Ms Zysman could become Mrs Abbott. But by adulthood the damage has already been done. Parents could change their names to give their children a better start in life. But a class made up only of little Aarons and Abbotts could be horribly confusing.

It would be hard, perhaps impossible, to stop alphabetism. But do not give up hope, all you Ps, Qs and Ws. The alphabetically disadvantaged may not become presidents, central bankers or rich, but they seem to thrive at running firms. Nine of the world's ten biggest companies (by revenues) are run by bosses with names that begin in the second half of the alphabet. An old theory thus gains credence. Only those who have battled against the odds will really make it in business.

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Japan

The shadow of joblessness

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From The Economist print edition

Rising unemployment is necessary, if Japan is to reshape and recover. But it is not sufficient

ANOTHER week, another set of impressive-sounding, or painful-sounding, job cuts from one of Japan's finest high-tech exporters. Last week it was Fujitsu, the country's top computer firm, cutting 16,000 jobs; this week it was the turn of Toshiba, a maker of memory chips, laptops and much else, to declare its plan to cut 19,000 jobs. Other cuts have come from NEC, a big telecoms and chips firm, and more are rumoured to be on the way from Hitachi, one of the country's older conglomerates (see article). The whiff of change is in the air: along with a new, reformist, no-gain-without-pain prime minister, Junichiro Koizumi, perhaps corporate Japan is starting to restructure, shedding its old lifetime employment rules and shaping up for a more vigorous future?

Alas not. Or at least, not yet. These big job-cut announcement have more of the old Japan about them than the new. Lifetime employment is still being protected: Fujitsu's cuts were mainly overseas, and Toshiba's are being phased in over three years. The pain is being borne mainly by the new school-leavers and graduates who will not now be recruited, rather than by higher-cost workers, who will be retained. Thanks to new consolidated accounting rules, there is less shuffling off of redundant workers to travel agencies or other make-work subsidiaries than might once have been the case. But these firms, and others among Japan's big battalions, remain unwieldy conglomerates doing far more tasks than they can manage efficiently. Hitachi consists of more than 1,000 companies; Fujitsu of more than 500.

Too few jobs lost, but far too few created

The right place to look in order to understand what is happening in Japan is at the broader picture. And that picture is looking steadily worse. If deregulation and real corporate restructuring get going, a time will come when rising unemployment and job-cut announcements are actually good news rather than bad, because they will indicate that change really is under way—as they did, in the 1990s, when countries in Central Europe were switching from communism to capitalism. Japan, alas, has not yet reached that point in its own transition from sclerosis back to capitalism. This week, the official unemployment rate rose to 5% of the labour force, the highest since 1953. This is a sign of the collapse of smaller firms, where lifetime employment has never prevailed, and of falling demand—which is why the Tokyo stockmarket fell this week to its lowest level for 17 years, despite those big high-tech firms' apparently inspiring efforts to cut jobs and limit their losses.

On the face of it, the official unemployment numbers suggest that Japanese joblessness is only a little above that in the United States. Yet the true level of unemployment is thought to be much higher than the official figure, because many of those who have lost their jobs have either not chosen to, or been unable to, register for unemployment benefit. Total employment has been dropping speedily: since December last year 800,000 jobs have gone (on a seasonally adjusted basis); over the past four years, the total is almost 1.8m. Since December last year more than a million people have left the officially counted labour force.

Clearly, with the world economy no longer doing Japan any favours, this is a tough moment at which to be considering radical reform and restructuring, which is what Mr Koizumi has said he is going to implement. As regulations are shaken up and firms restructure, unemployment could rise far beyond current levels, depressing consumer confidence, prices and demand even more, causing more job losses

in an ever nastier downward spiral.

Tune in, reflate, start up

That is why, as well as his efforts to bring on the pain of restructuring, Mr Koizumi and his government need to keep their eyes on two other things. One is by now familiar: demand, which can be stimulated by an aggressive expansion in the money supply. The Bank of Japan has edged tentatively in this direction, but is still showing little enthusiasm for the task. There is some talk of direct monetary expansion by the Ministry of Finance, which it could achieve by borrowing directly from banks to finance its spending rather than (as is normal) from the bond market. But there is no sign of more than talk. If Mr Koizumi is not to lead Japan into a depression, he will need to take a strong personal interest in the money supply.

The second forms part of Mr Koizumi's plans for supply-side reforms. But it is too often overlooked amid all the talk of pain and purges. This is that, outside the financial sector, the main target of reform and restructuring must be the encouragement of new businesses and markets, and of new entrants to existing markets. Any economy can destroy jobs. It is much harder to create them, but if the rise in unemployment is to be limited and then put into reverse, that is what must happen.

It is often claimed that there is no real entrepreneurial culture in Japan, so all the new jobs will have to be created at existing firms. This is not true. Even well after the post-war age when the Sonys and Hondas were being founded, the flow of start-ups remained high in manufacturing, distribution and services all through the 1960s and 1970s. It was only in the 1980s that entrepreneurial activity really slowed down, presumably as many markets became gummed up by incumbents and by regulation.

Even now, amid a sliding economy, the fires of entrepreneurship are flickering. The number of initial public offerings on Japan's stockmarkets has been rising: there were 18 in July and 19 in August, and more than 20 are planned for September. Many more will be needed. If they are to come, then the government will have to force big, old dominant firms, such as NTT in telecoms and all the other big utility companies, to stop squashing innovation and new competition. Millions of jobs were destroyed in America by deregulation. But millions more were created by start-ups and by expansions of existing small and middling firms. That is what Japan must now do: free its budding entrepreneurs. Without them, the growing legions of the jobless will have little real hope.

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Letters

Aug 30th 2001
From The Economist print edition

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Bioethical issues

SIR – Your article on Leon Kass (Lexington, August 18th) is off the mark. Mr Kass acknowledges readily and frequently the promise and benefits of science. And your attempt to portray him as politically on the right is misleading. Mr Kass's personal style and nuanced perspectives transcend simplistic political caricatures. Moreover, despite more than three decades contemplating bioethics, he remains reluctant to posit answers to the moral questions raised by modern science.

Most importantly, Mr Kass's "wisdom of repugnance" is not an argument that implies we ought not to overcome fertility or cure a crippling illness because envisioning humans with horns, wings, gills and tails is discomforting. Rather, it is a thoughtful acknowledgment that in the face of a sometimes overwhelming and often unquestioning drive toward medical progress, human nature still provides us with an emotional mechanism to help decipher right from wrong. Mr Kass rightly argues that this mechanism tells us that we ought not to be complacent about what is at stake, for where our reason may find excuses to justify complacency, our repugnance cannot.

Martin Stein
Lake Forest, California

SIR – I am delighted that Mr Kass has been influenced by C.S. Lewis's "The Abolition of Man "—but disappointed by your account of this influence. What worries Lewis (and Mr Kass) is not the blessings of science, which few cannot admire, but the effect of scientific progress on our ethical thinking. This has not only resulted in more blessings (with occasional slips, like the atom bomb) but has helped to make what you call "a society that tends to reduce all choices, however profound, to the level of consumer preferences." Lewis envisaged a hypothetical future when ethical norms are not just chosen but produced, manipulated and changed at " will" into anything we humans "want". This would mean what Lewis called the abolition of man (ie, of humanity) because there would be nothing left of human motivation to distinguish it from that of animals.

Thus, Lewis throws light on the nature of ethics. This hypothetical future will be either impossible or repellent, underlining a distinction that has, for all practical purposes, been progressively blurred by the progress of science. Ethics, including bioethics, is not what we choose but on what we base choices. Ethics may be both more difficult and more interesting than simply increasing people's choice and freedom of choice; it may also be more important. Anyway, it is something quite different.

Arend Smilde
Utrecht

Soviet-era debt

SIR – Your account of Russia's dealings with Noga, a Swiss trading company, is inaccurate ("Pay up", June 30th). Noga sought over $1 billion in arbitration. The arbitrators awarded Noga $48m plus interest and found that Russia did not cause Noga's financial difficulties. Recognising that Russia cannot honour its Soviet-era debts, Russia's Paris Club and London Club creditors have restructured almost $60 billion of debt. Russia has agreed with the Paris Club not to grant preferential terms to any other creditor. Russia also recently agreed restructuring terms for its Soviet-era trade debt with creditor representatives in 12 countries, including Switzerland, and has invited Noga to participate in this restructuring. Noga's insistence on full payment in preference to other creditors is ironic given that in 1998 Noga discharged

under Swiss bankruptcy law its own debts at 12.78% of their face value. These debts included tens of millions of dollars of damage awards held by Russian companies.

The Russian government is strongly committed to the rule of law. This principle is a two-way street. Noga's recent attempts to attach military aircraft is only the latest example of its repeated abuse of the legal system to attach assets improperly that are either immune from seizure or do not belong to the Russian government.

Sergei Kolotukhin
Deputy finance minister
Moscow

Non-return of the native

SIR – As a native Iowan living in London for the past nine years, I read the article on Governor Tom Vilsack's plan to persuade people to live there with interest ("Fare thee well, Iowa" August 18th). As one of the people he may be interested in reaching, I suggest that Iowa lacks a diverse and dynamic culture, and until that problem is addressed no one will be attracted. Iowa does have high social capital (good schools, short commutes, little crime and cheap housing) but there must be a high correlation between such a measure and what I might call unscientifically a boredom index. Resident Iowans need to be less socially conservative and more welcoming to new ideas about what is culturally valuable; only then will people consider Iowa as a place to live and work.

But I grant you that Mr Vilsack will not be too worried if his plan fails to attract people to Moline. It is in Illinois.

Bryan Brinkley
London

Road safety in Brazil

SIR – As a Sao Paulo resident of three years, it is important to point out that the level of nervousness about the violence here is not directly related to the actual threat of attack ("Bullet-proof in Alphaville", August 18th). Sao Paulo's inhabitants suffer from a high degree of urban paranoia stemming from the knowledge of the huge gap between rich and poor in Brazil, and the underclass that this creates. Also, it is increasingly "chic", as well as a sign of wealth, to bullet-proof your car. Paulistanos are notoriously vain, and particularly image conscious.

Around 80% of all violent crime here occurs in the *favelas* (shanty towns), fuelled by drug dealing, drinking and poverty. Middle-class Paulistanos never go anywhere near *favelas*, even though their maids and drivers probably live in one. The middle classes would prefer to forget about this situation, rather than pay more taxes to rectify it.

Gail Mowat
Sao Paulo

SIR – You consider security, just one aspect of the inability of the Brazilian government to perform its basic functions. Education and health care are other areas in which affluent Brazilians have chosen private provision over poor state services. The feeling is that everybody has to look after their own well-being, regardless of the rest. This could end with the complete failure of the government to create an environment where society can discuss and agree on minimal common goals.

Gabriel Priven
Sao Paulo

Landmark decision

SIR – If the European Union wants to promote a visible feature of Brussels, I can think of none better than the Grand Place ("A bureaucracy by any other name", August 4th). The present EU leadership would probably not be enamoured with a marketplace as its symbol. However, it should be mollified by the fact that the Grand Place is surrounded by guildhalls, symbolically guarding against any meaningful forms of free enterprise.

Roger Foster
Alexandria, Virginia

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The Baltic states

Knocking at the clubhouse door

Aug 30th 2001 | RIGA, TALLINN AND VILNIUS
From The Economist print edition

The Baltic states of Latvia, Estonia and Lithuania are close to joining the European Union and, perhaps, NATO too. How ready are they?

A COLOSSAL ruined satellite dish and a cluster of derelict antennae deep in the Lithuanian countryside are the only remaining sign of the Linksmakalnis listening station, once one of the Soviet Union's most secret military installations in the Baltic states. The locals say hundreds of people once worked there, scouring the airwaves for secrets from Western Europe. To this day, officials cannot (or will not) say exactly what went on there.

A few miles away a new lot of electronic snoopers are hard at work, but in the other direction. Radars all over the Baltic states, looking hundreds of miles deep into Russia and Belarus, beam data to powerful computers housed in a former Soviet nuclear bunker. Projected on to a giant screen in the control room are the results: the movements and identities of every aircraft in or near the region.

Not that the watchers can do much about what they see, since the Baltic states have no combat aircraft to scramble against an intruder. But it is a start: it shows that the Balts are not just consumers of western security, but also providers. At a touch of a button the Baltnet system hooks up with similar radars in nominally neutral Finland to the north, and with NATO's own eastern defences to the south. Even from outside NATO, the Balts can lend a human and electronic hand to the alliance.

The Baltic states are hoping that projects like Baltnet will help their cause in the coming months, as NATO decides whether to include them in the next round of enlargement, or keep them waiting. Of late, the argument has shifted a bit in favour of the Balts. But the worriers go on worrying. Latvia, Lithuania and Estonia are three small new democracies, containing between them less than 8m people. Stuck between the Baltic Sea and Russia, they strike sceptics as indefensible. Their armed forces are still weak. Is it worth antagonising the Kremlin for their sake?

The question is what Russia would really do. President Vladimir Putin sounds less hawkish on this than some of his officials. He claims not to understand NATO's thinking, but reacts to talk of enlargement more in sorrow than in anger. Vyacheslav Nikonov, a political analyst close to the Kremlin, says that if expansion went ahead Russia would strengthen its forces in the Baltic region and perhaps even put nuclear weapons in Kaliningrad, the cut-off patch of Russia that lies to the west of the Balts. That would indeed be a show of force; but it would be one the rest of the world could probably live with.

The three Baltic governments are eager to join the club. They have shown that they are prepared to spend a big share of their puny budgets on defence: fully 2% of national income. Hundreds of millions of dollars-worth of donated Swedish equipment will add beef in the coming years. The Balts may not be able to afford jet fighters, but they will have runways and hangars that can accommodate NATO ones.

The Balts' cause is helped by Russia, which has misplayed its hand. The Kremlin claims at one and the same time that it poses no threat to the Baltic countries (and so NATO membership is unnecessary for them) but that its special interest in this region, as a chunk of the former Soviet Union, should be respected (therefore NATO membership is an insult to Russia). Enforced respect and unwanted influence are exactly the threats from Russia against which the Balts want NATO protection.

Indeed, the Russians may hurt themselves by what they are doing. The Lithuanians, who sit next to Russia's outpost of Kaliningrad, say that many of the Russians now running Kaliningrad are far more relaxed about their territory's relations with the surrounding parts of Europe than their predecessors were a few years ago. They want to trade with their neighbours, and to let workers and capital move relatively freely across the region's borders. The government in Moscow is therefore running a large risk. If it stays cold towards the Balts, it may find that Kaliningrad, though still formally part of Russia, is in fact developing closer links with the rest of Europe than those it has with its old motherland.

If Russia stays cold towards the Balts, Kaliningrad may slip slowly away

If NATO does take in one or more of the Baltic states, some juicy arms contracts will result. The main contractor for the $100m Baltnet radar was Lockheed Martin, one of whose senior executives also leads the main lobbying group for NATO enlargement. There is growing American enthusiasm for spreading NATO wider. Yet a fair question remains. Is America really prepared to stretch its nuclear guarantee to the Baltics, as it once covered Western Europe? Even if the answer is "probably not", new members so far have not insisted on a specific commitment on this point. They live in hope.

Stylish deception

Membership of that other club they keenly hope to join, the European Union (EU), is a more pressing issue. Although all three countries have made impressive progress in the past decade compared with other ex-Soviet countries, big problems persist.

A few locally managed businesses compete well in international markets (an Estonian firm that makes cross-country skis, for example, and a world-class software company in Latvia). Tallinn, Riga and Vilnius are deceptive showcases for their countries; tourists and visiting officials alike are charmed by the architecture, wowed by the multilingual friendliness, seduced by the good restaurants and hotels. But at the outskirts of the capitals the prosperity fades out in bleak housing estates, tatty factories, bumpy roads. Out in the countryside, particularly in Latvia and Lithuania, things look even worse. As in Russia, villages suffer from poor public services, depopulation and alcoholism.

The smallholdings that have replaced Soviet-style farming are picturesque, but mostly unable to provide their owners with more than a subsistence income, $100 a month or less. The powerful pre-war producer co-operatives that made Baltic butter and pork into thriving industries are all but forgotten. Country towns are poor, and offer few jobs. Even in Estonia, the smallest and most prosperous of the three countries, there are big differences of wealth. The average gross monthly wage in Tallinn at the end of last year was $359, compared with $205 in Voru County in the much poorer south-east.

Even with fast economic growth, it will be decades before the southern side of the Baltic Sea catches up with the countries on its northern and western shores. To reach even half of the EU average by 2010, Estonia's GDP per person would have to increase by 5-6% every year for the next ten years. At current rates, it would then reach $15,000. Lithuania, on present form, would reach only about $6,000.

There is also, in one way, a growing sense of isolation. The number of people who can speak or understand Russian has fallen sharply, and many youngsters do not even try. But little else has arrived to replace Russian. Outside the big cities, English has made only limited inroads. Other foreign languages (even the next-door neighbours') are scarcely spoken at all. This is a pity. Small countries need to be polyglot to prosper.

The continuing economic bleakness also creates a political problem. Ten years ago, people were remarkably willing to trust their politicians. Having risked

Ten years ago,

death or deportation to be free of Soviet rule, they were ready to accept wrenching economic changes. But the rulers of all three countries were largely unprepared for the challenges of the post-cold-war world. Ex-dissidents often proved quarrelsome and ineffective in power. Ex-Soviet types brought their own bad habits from the past: greed, bossiness, secrecy.

people trusted their politicians. Today, it's back to corruption and incompetence

The resulting corruption and incompetence have squandered much public trust. Dodgy privatisations, too much evident self-enrichment and an alarming inability among politicians to communicate with the voters have left many people feeling tired and cynical. Even in Estonia, where to outside eyes the government is talented and reform is successful, many ruling politicians are accused of being arrogant and sleazy. Some Balts are voting with their feet. In Lithuania, one senior government figure reckons that as many as 200,000 of its 3.7m people have emigrated since independence, most of them young.

Sloppy government also makes it hard for foreigners to trust the Balts, even when they like them. Finland, for example, has equipped and trained Estonia's border guards well; the radars are so sensitive that they can spot a fox crossing a frozen lake. The relationship between the two countries is, in general, a model for post-communist Europe. But large quantities of heroin and amphetamines still get through to Helsinki from Estonia. Problems like this have to be solved before the Baltic states can become members of the EU.

Primping for the EU

In theory, joining the EU should solve the Baltic states' internal troubles, just as they hope that joining NATO will settle their external ones. At the moment, Estonia is seen as one of the best-qualified to join the EU, along with Slovenia and Hungary. Latvia is gaining ground. Lithuania is still lagging behind. In GDP per person there is not much of a gap between the three. The striking difference is in trade and investment. In Estonia's open economy, foreign trade as a percentage of GDP is about twice Latvia's and Lithuania's (see table), and its foreign direct investment per person is higher too.

How they're doing
2000

	GDP, $bn at PPP*	GDP per person, $ at PPP*	Trade balance, $bn	Trade, % of GDP	Foreign direct investment inflows, $ per person
Estonia	8.7	6,040	-0.79	148	179
Latvia	11.4	4,802	-1.06	72	170
Lithuania	17.1	4,609	-1.10	82	102
Russia	722.0	4,970	60.70	60	19
Greece (for comparison)	171.0†	16,200†	-20.23	36	107†

*Purchasing-power parity (PPP) seeks to equalise the prices of identical bundles of goods and services in each country †Estimate
Sources: Economist Intelligence Unit; IMF

Still, it is a fair bet that all three will join the EU together. Drawing a line between the Baltic states, only to remove it a couple of years later, would make no sense. As with other applicant countries such as Hungary and Poland, a slice of EU structural funds (money for roads, bridges and the like) would be welcome. Full access to the single market will help to make companies more competitive. European levels of efficiency in government, particularly in the legal branch, are much needed.

The easy negotiations have happened already; the difficult ones are mostly yet to come. Officials in Tallinn are furious that most EU countries are refusing to open their labour markets to even a trickle of Estonian workers. In Estonia, particularly, preparing for EU membership has sometimes meant reducing standards, not raising them. Lamentably, Estonia has had to introduce import tariffs and agricultural subsidies, two bad habits which its zealously free-trading government had scorned in the early years of reform. Estonian officials hope that, once inside the EU, they can add their bit to the lobby for freer trade and less government interference.

There is less Euroscepticism among the Balts than among the other applicants, because the alternative is so bleak. If EU membership were delayed, joining NATO would be impossible. However harsh, slow and cumbersome the Euro-accession procedure, few Balts want to risk being in the same boat as Moldova or Morocco.

The Russian shadow

Another difference from other would-be EU members is that the Baltic states bring with them a number of unsolved questions about Russia. One concerns potentially disputed borders. This is a particularly prickly issue for Estonia, which, like Latvia, lost some of its eastern territory to Russia during the Soviet era. Estonia has given up any claim to these slivers of land, now mainly filled with Russians, but the Kremlin will not ratify the border treaty.

Lithuania's position is different. Whereas Latvia and Estonia lost territory under Soviet occupation, Lithuania gained a lot, chiefly the historic capital, Vilnius (under Polish rule until 1939), and the main port, Klaipeda (formerly Germany's Memel). When the Lithuanian parliament last year voted to demand compensation from Russia for losses during the Soviet occupation, some politicians in Moscow were quick to suggest that Lithuania should give back what it had been given.

These are not live issues at the moment. But in a few years' time—perhaps as soon as 2004—the Balts' eastern borders will also be the EU's. Kaliningrad will then be entirely surrounded by EU (and perhaps NATO) territory. That raises big and unanswered questions about visas, trade and security. So far, Russia seems to see Kaliningrad not as a way of building a bridge for itself into Europe, but as a bargaining chip over the future of the Baltic states: which could prove a big mistake.

Unlike any of the other applicants, the Baltic countries will bring a large number of ethnic Russians—about 1.5m, a fifth of their total population—into the EU. Around 150,000 of these are citizens of Russia itself; about half are citizens of the Baltic states, either because their families were citizens before 1940 or because they have acquired citizenship by marriage, or through naturalisation. In Latvia and Estonia, naturalisation mainly involves passing a language test; in Lithuania, where the Russian population was less than 10% at the time of independence, citizenship was granted automatically.

The remaining 700,000-odd people are, in effect, stateless. They lost citizenship of the Soviet Union when it collapsed, but either from apathy or out of principle have not tried to become either Russians or citizens of their new countries. They and the citizens of Russia are barred from some occupations, and cannot vote in national elections. The Kremlin calls this unfair. Estonia and Latvia (and, mutedly, the West) argue that giving Soviet-era migrants the same rights as the people they had colonised would be even more unfair.

On paper, these look like serious problems. The Baltic states are ethnically divided. Groups of people stranded when empires collapse, especially if they lack full economic and political rights, bring ominous historical echoes—like the Germans in Czechoslovakia's Sudetenland, whose supposed plight was a pretext for Nazi aggression.

In fact, Russia's stranded Baltic colonists are no great cause for concern at the moment. For all the economic problems in the Baltic states, living standards are much higher there than in Russia. Some Russians who left after independence are now trying to come back. Political conditions are improving, too. Estonia and Latvia have softened their language and citizenship laws to the point where the Organisation for Security and Co-operation in Europe, the main body dealing with the issue, is getting ready to close its local offices.

Attitudes have changed as well. As memories of the forced migration of the Soviet era fade, Estonians and Latvians have stopped assuming that the "Russian occupiers" will "go home". For their part, the local Russians seem willing to accept Baltic independence as a fact. There is much more readiness, especially in Latvia and among young Russians in Estonia, to learn and speak the local language. Nationalist tub-thumpers from Moscow find almost no local echo. To the extent that Russians living in the Baltic countries look for outside help, they look to Brussels, not Moscow. Integration could go a lot faster, but, for the most part, time is solving the problem. Some of the Baltic Russians call themselves *Yevrorussky*, Euro-Russians. If only Russia itself would think along those lines a bit more.

No other EU applicants have suffered the trauma of full-strength

The biggest problem for all the Baltic states is a different one: tackling the Soviet legacy. No other country likely to join the EU in the near future has suffered the trauma of full-strength Stalinism. These three were part of the Soviet Union itself, not just the region it controlled. "Estonia will soon be ready for Europe as a state, but it is far from being ready as a society," a perceptive journalist, Andres Langemets, wrote last year. Egidijus Aleksandravicius, who runs a Lithuanian foundation, says of final-year university students that "80%

are still socialist-minded...For them, the state is extremely important and responsible for everything; personal responsibility is very weak."

Working that out of the system will be tough. But it will be a lot easier if the Baltic states are safely anchored in a democratic, prosperous West while they get on with the job. They are close to being so; and, given their battered history and precarious geography, that is more than most people hoped a mere ten years ago.

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The growth of private communities

America's new Utopias

Aug 30th 2001 | ANTHEM, IRVINE, LEISURE WORLD, SUN CITY AND VALENCIA
From The Economist print edition

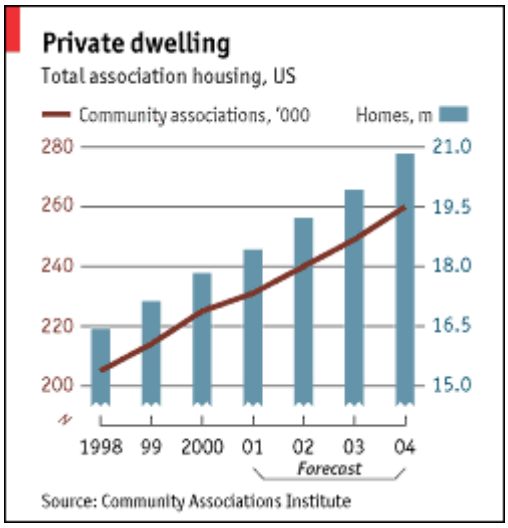
Private housing associations increasingly lay down the laws that middle-class Americans live by. What are they doing to the country?

HEAD north out of Phoenix, Arizona, up the I-17. Drive past the signs for Happy Valley Road, Carefree Highway and, less auspiciously, one advising you not to pick up hitchhikers because you are passing a federal prison. Eventually you come to one for "Anthem by Del Webb".

Anthem feels more like a luxury holiday resort than a town. It includes a water park, with Disneyesque water slides, a children's railway, hiking trails, tennis courts, a rock-climbing wall, two golf courses, several spotless parks, a supermarket mall, two churches, a school and, for those who want a little more security, the Anthem Country Club, a gated (and guarded) community.

Anthem, which is planned to have 12,500 homes, opened in 1999. Its houses and roads look spotless. One reason for this is that everybody who buys a house in Anthem has to follow certain covenants, conditions and restrictions (CC&Rs), governing everything from the colour of your house to whether you can put your car on blocks outside it (you can't). Everybody in Anthem, except the construction workers, seems to be white.

Anthem sounds like an exclusive enclave for the rich. Far from it: homes start at a distinctly modest $155,000. Even the residents of the Anthem Country Club hardly seem posh. They tend to laugh at the rules, regarding them, like the long commute to Phoenix, as part of the price. Why did one young mother come here? "Because it's safe, because there are activities, because it's, well, like us."



Indeed, Anthem is not bucking a trend, but joining it. In many of the fastest-growing parts of America, development is being driven by "master-planned communities" of one sort or another. In big cities half the new home sales are in association-managed communities, according to the Community Associations Institute. Altogether, some 47m people—one in six Americans—live in 18m homes in 230,000 communities and pay around $35 billion in fees every year. Around 1.25m people serve on community-association boards.

Nowadays, whoever you are, there is probably a community planned with you in mind. In Nevada, a 55-acre community called Front Sight, featuring streets with names like Second Amendment Drive and Sense of Duty Way, is being built for gun enthusiasts (people who buy an acre plot get lifetime use of the 22 planned ranges, an Uzi machinegun and a safari in Africa). In Baton Rouge, Louisiana, one gated community seems to have been taken over by black rap stars. In poor areas of Chicago, residents have set up gated communities to ward off crime. Though most of these places are in the west and the south, they crop up all over the country.

Legally speaking, there are three different kinds of association. The commonest, about 60% of the total, are home-owner associations: a house buyer also becomes a member of an association that owns the

common areas, levies dues and sets rules. Another 30% or so are condominiums—typically flats in a single building—where the whole building is owned by a condominium association. The remaining 8% are co-operatives, which are like condos, except that the owners have shares in the co-op; most of these are in New York. Of all these, some 20,000 units, housing 8m people, are gated communities.

The CC&Rs vary. In some cases, they just govern how you sell your house. But the list of rules seems to be getting longer. Some residents have to cough up for maintaining the roads, pavements and street lights, looking after the parks and providing security. A maximum size for dogs—usually 30lbs—is increasingly common. Leisure World, California, has its own television station. The proliferation of CC&Rs is driven by the trend towards master-planned communities (like Anthem), where the developer tries to create not just a cluster of homes but a way of life.

The two models for master-planned communities both date back to the 1960s: Irvine, in southern California, and Sun City, outside Phoenix. The whole of Irvine was built by one firm, the Irvine Company, which says confidently that its present population of 200,000 should double in the next 20 years. The company presides over Irvine in an avuncular manner. Apart from laying down the CC&Rs, it lures in businesses (the Irvine Spectrum business park is one of the fastest-growing in the country), and in 1961 it gave 1,000 acres to set up the local branch of the University of California. Irvine's 75,000 homes are divided into 25 villages (some gated, most not) which collect the dues and watch over the rules.

The result, argues the Irvine Company, is "smart growth". Whereas many Californians spend hours commuting in their cars, 60% of Irvine Spectrum's workers live within 15 minutes of their jobs. Unplanned towns tend to eat into parks, but 40% of Irvine's space will remain unbuilt-on forever. And then there are all those nice little things. Graffiti are quickly removed; there are no billboards on the freeways; construction workers have to spray water to keep down the dust.

Sun City, the other great model, is a town of 46,000 people built by Del Webb on the other side of Phoenix from Anthem. This is a retirement community, still probably the main section of the market. Retiring to one of these communities (Sun City alone has bred a dozen places with the same name) has become almost a routine part of middle-class life.

Many of these towns require at least one person in each house to be 55 or older, and exclude children. Leisure World, another pioneer from the 1960s, has 20,000 people with an average age of 77. The west is littered with elderly Chicagoans who left the Windy City because of the cold and now can't stop moaning about their air-conditioning bills. Even Rabbit Angstrom, John Updike's American Everyman, ended up in a Florida condo.

But the retirement market is changing. Witness the newest Sun City outside Phoenix—a computerised, Starbucked, multi-gym affair aimed at "active adults". By 2010, there will be 75m Americans aged 55 or more. People now live about 15 years longer than when the first Sun City was built, but most of the surge in numbers by 2010 will come from the 76m members of the baby-boom generation, now moving towards retirement.

The older sort of retirement community is not exactly a senile nursing home (there were two dozen complaints about couples having sex outdoors at Sun City West last year, the average age of the offenders being 73). But the baby-boomers represent a new challenge. Zoomers—Del Webb's name for the first group of retiring boomers—prefer to retire early (Del Webb's research shows one in three planning to retire before 60), but without giving up work completely. Retirement for them will be a third age, still full of assorted activities.

Why they keep growing

Demographics partly explains the growth of planned communities. But there are two deeper forces at work: American Utopianism, and distrust of government.

Evan McKenzie, a professor at the University of Illinois in Chicago and author of "Privatopia" (Yale University Press, 1994), argues that, whereas European Utopians tended to concentrate on changing the society around them, American ones preferred to go off and create a new world somewhere else. Some cities-on-a-hill have been built by religious fervour. More often, immigrants simply want to use America's empty space to create a better life. Contemplating the "uncontaminated" wilderness of the west, Thomas Paine once mused, "We have it in our power to begin the world all over again."

A similar optimism, if not quite so elegantly phrased, litters the literature of planned communities. The other side of the coin is pessimism about—and often disdain for—the services that public cities provide. The commonest worry is security (hence all those gates, though there is not much evidence that gated communities are safer than non-gated ones). But there are also concerns about education, health care, transport: everything the public sector is supposed to provide.

Compare Valencia, a fast-growing "private" city an hour north of Los Angeles, with the San Fernando Valley, which is the northern part of that city, and has provided around a quarter of Valencia's 42,000 people. Children in the San Fernando Valley are condemned to schools run by LA's notorious Unified School District; Valencia's schools are excellent. People walk in the Valley only if they run out of petrol; Valencia has 25 miles of *paseos* for people to jog and bike along. Crime is high in the Valley; Valencia is part of Santa Clairita, one of the safest cities in the country. Thanks to smart growth, two-thirds of the homes in Valencia are within a quarter of a mile of school, shops and library. If only, moan Angelenos.

Joel Kotkin, author of "The New Geography" (Random House, 2000), calls the rise of places like Valencia "an escape to sanity" from the corruption and inefficiency of big-city government. Community associations took off in California in the 1970s, the same decade as the passing of Proposition 13, which cut taxes for local government. And their growth has also coincided with that of private schools and private security guards; the latter now outnumber the "public" police by four to one.

So are planned communities a good thing? For the Americans inside them, the answer is usually yes. "Do I like being told that I have to warn the security guards that I am going to have a party, or that I cannot put up a basketball hoop in my driveway?" asks one Irvineite. "Of course I don't. But it's not something that keeps me awake at night." There is a widespread feeling that housing-association boards attract the worst busybodies in town. Yet still the queue of applicants goes on growing.

The public-private schism

What about America as a whole? These are, still, mainly white places. In five days *The Economist* met only one black resident and no Latinos in a string of planned communities across the west and the south-west. This may change, as America's middle class grows steadily more multi-coloured; but for now the juxtaposition of white Sun Cities and Latino local schools in Arizona is strange, even troubling.

A more general worry is that a growing part of the middle class is abandoning the state: living on private roads, sending its children to private schools, paying for its own private police force, playing golf at private clubs. Why bother supporting public services when you get all yours delivered privately? And what about all those poorer people, stuck with public housing, public schools and public transport? From the right, Charles Murray has talked of America's coming "caste society", with old-style cities becoming like Indian reservations. From the left, Robert Reich fears a secession of the successful.

This is an exaggeration. There are occasional examples of selfish behaviour: some elderly gated communities have voted not to let public schools within their walls. But there is no evidence that whites in planned communities are any more hostile to government spending than those outside. The mayor of Irvine, Larry Agran (a left-wing Democrat who once ran for president), says the people of Irvine are far more involved in both their state and local governments than people in Los Angeles, where he used to live.

To be sure, the growth of planned communities can eat into the authority of the state. Robert Nelson, of the University of Maryland, points to two examples. The CC&Rs trump a good deal of municipal law (for instance in terms of property-sales contracts). Second, a community can set rules about who is allowed to live in it.

For Mr Agran, all this is worthwhile. The real evils of life in southern California, he says, are things like "the separation of the workplace from the home". In communities with smart growth this is a fading problem. Mr Kotkin agrees: "It would be perverse to limit the growth of successful places that people want to live in."

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The economy

Home is where the wealth is

Aug 30th 2001 | NEW YORK
From The Economist print edition

Rising house prices, not share prices, have been fuelling consumer spending. But for how much longer will prices go up?

IF AMERICA'S economy avoids sliding from downturn into a full-blown recession, it will be because the consumer continues to spend freely. Some economists had feared that this week's revised GDP figures would show that the economy had shrunk in the second quarter. Instead, consumer spending kept the figure positive—albeit at just 0.2% compared with the previous quarter at an annual rate.

Consumer spending, which accounts for two-thirds of economic activity, has remained strong despite falling share prices and rising unemployment for one main reason: a housing boom. Average house prices rose 8.8% in the year to March. New government figures, due this weekend, should still show an upward trend.

True, house prices have softened in areas most exposed to the "new economy" (remember that?), such as Silicon Valley, San Francisco and New York. There has also been a drop at the other end of the market: defaults on mortages on mobile homes have risen sharply. But, strange though it may seem, neither Manhattan apartments nor Arkansas trailer parks are representative of the country at large. According to the National Association of Realtors, the median existing-home price in the second quarter of this year was $146,900, up from $138,000 a year earlier.

Among metropolitan areas, Sacramento had the biggest price increase, up by 23.9% year-on-year, followed by Washington, DC, (18.6%) and the Bergen-Passaic area of New Jersey (17%). Regionally, the fastest growth is in the South, up by 10.2%, compared with 1.4% in the north-east. House sales nationwide are expected to reach record levels this year.

The housing boom fuels consumption in several ways. When people move, they tend to buy durable goods such as furniture, fridges and carpets. Lower mortgage rates—down to an average of 6.9% on a 30-year mortgage from 8.6% in May 2000—have prompted many homeowners to refinance on better terms, putting money in their pockets. After slowing down in recent months, refinancing has started to surge again in the past couple of weeks as mortgage rates have edged below 7%.

Higher house prices make homeowners feel wealthier and so more willing to spend. For all the attention given to the "wealth effect" on consumption of rising share prices, the housing wealth effect is better understood, stronger and more broadly based. The stockmarket's rise and fall mainly influenced spending by the richest Americans, who own most of the shares. But for most Americans, their house is their main asset. It has become easy for them to turn an increase in the value of a house into spending money by

taking out a home-equity loan. And even though they have been doing that in droves, most estimates show total unrealised home equity has continued to grow.

Alan Greenspan, the chairman of the Federal Reserve, recently said that this unrealised capital gain was not “a depleting asset”. Paul McCulley, an economist at PIMCO, a bond fund-management firm, reckons that this was a hint that the Fed chairman would try to keep house prices rising, come what may. Can he do it?

Mortgage rates have not come down by much since January, when Mr Greenspan began his run of seven cuts in short-term rates. That may be because the market had already anticipated these cuts. But mortgage payments as a proportion of disposable income have edged up to 6.5%, from a low of 5.6% in 1994.

Charles Peabody of Ventana Capital, a research firm, points out that houses are taking longer to be sold and that there are more sales at below the asking price (the norm until recently was for the final price to be higher). Second homes and high-end housing are especially weak on these scores. “We are at the inflexion point,” Mr Peabody claims.

But the bulls have their own figures. Ian Shepherdson of High Frequency Economics, a research firm, says house prices will rise as long as interest rates do not. Currently, “it is an absolute no-brainer to gear up and buy a house,” because the rate of increase of house prices is higher than the mortgage rate. This has usually been a good leading indicator of further rises.

Might higher unemployment swell the number of houses being put up for sale and thus dampen prices? Only a bit, argue the bulls, because supply is so tight. In the past, housing booms have been killed only by rising mortgate rates, argues Mr Shepherdson. Nobody expects that to happen again soon. Hence the hope that the home-owning consumer will continue to spend the economy out of trouble for long enough for the corporate sector to sort out its problems. That may be what Mr Greenspan is betting on, too.

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United Nations dues

Tremble, Holland, tremble

Aug 30th 2001
From The Economist print edition

America's odd attitude to international institutions reaches new heights

GEORGE BUSH'S first speech to the United Nations, scheduled for September 24th, may prove an embarrassing one. After all the ballyhoo about the United States at last beginning to pay some of the $2.3 billion it owes the UN, Mr Bush's own party has thrown a spanner in the works.

Back in 1999, Congress passed the Helms-Biden act, which promised to pay $1 billion in arrears, subject to various UN reforms. (Incredibly, getting the richest country in the world to pay half its debts was considered a triumph for the UN; plenty of impoverished places pay on time.) A first slab of $100m was paid out late in 1999. A second payment of $582m was due in December 2000, when the UN agreed to revise its budget quotas, so reducing the American contribution to its regular budget immediately from 25% to 22% and to peacekeeping gradually from 31% to 27%.

The latter was legally awkward because, back in 1994, Congress had unilaterally decided to cap its peacekeeping contribution at 25%. (This partly explains its arrears.) In order to release the $582m, Congress had to revise the Helms-Biden act to raise this number to the UN's new cap. The Senate did this in February; but for the UN to get its money, the House needs to do the same.

Trouble has sprung up because the House Republican leaders want to add some new conditions, linking the payment of arrears with a bill that seeks to protect American soldiers from the International Criminal Court. (The ICC is not a UN body, but if you are a conservative congressman, the tribunal is still part of the new world order.) In his last days as president, Bill Clinton signed the Rome Convention setting up the international court in The Hague; but, as Mr Clinton well knew, the decision is unlikely to be ratified by Congress or Mr Bush any time soon.

Under the Republicans' American Servicemembers Protection Act (ASPA), the government would suspend military assistance to any non-NATO member joining the ICC; refuse to co-operate with the tribunal; decline to take part in UN peacekeeping operations unless the Security Council exempts American soldiers from possible prosecution under the ICC; and authorise the president to send troops to release Americans or allies held by the international tribunal. "The Hague Invasion Act", as critics have dubbed it, has not gone down well with allies.

It also has yet to get anywhere in the Senate, despite Jesse Helms's support. But the act's provisions were passed by the House in May as part of the State Department appropriation bill—which also included the provisions for the payment of UN arrears. Mr Bush and the Senate are keen to keep the issues separate. They are thus putting pressure on the House to pass the revised Helms-Biden bill, so that the money can be paid out immediately.

Negotiations are continuing. But there is not much time to achieve a deal before Mr Bush's speech on September 24th. If the House refuses to compromise, the UN money will await a compromise on the State Department appropriation act, which could take much longer.

Even if the $582m is released, America's squabbles with the UN are not over. Earlier this year, America was kicked out of the UN High Commission for Human Rights, and furious House members have demanded redress for this affront before the final payment of $244m—scheduled for next year—is released. The UN may wait for its cheque for quite some time.

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About sponsorship

In the wild

The trouble is, people get there

Aug 30th 2001 | BRIDGER LAKE
From The Economist print edition

America's remotest spot

WHERE is the remotest corner of the United States, outside Alaska? If you are looking for the place farthest away from houses, head for somewhere near Escalante, in southern Utah. But, in terms of distance from the nearest road, Cartographic Technologies, a Vermont firm that had to come up with the answer for a Land Rover advertisement, gives the prize to Bridger Lake, in Wyoming, in the northern Rocky Mountains.

The lake is small, clear and surrounded by shores dotted with bluebells and trees (many, alas, blackened by the 1988 Yellowstone fire). The mountains above, which look like giant pin-cushions made of green velvet, form a valley known by local people as Thorofare County.

It is a 32-mile hike, by mule or foot, from the nearest publicly maintained road to Bridger Lake, though crows and eagles can make it in 20 miles. The lake is a mere five miles from another cartographic marvel, the Parting of the Waters at Ocean Creek—the only stream in the country to feed both the Atlantic and the Pacific. Because Thorofare is at the northern end of the vast Teton Wilderness (which takes in an area much larger than the Teton National Park), Bridger Lake is protected by Congress from chainsaw and miner's drill. The nearby Yellowstone, which flows into Yellowstone Lake, is one of the last undammed rivers in the west.

But remote, nowadays, does not mean untouched. "The Thorofare is an extremely popular destination," sighs Ron Paris of the US Forest Service Buffalo Ranger District, which looks after the area. Others less politely say it reminds them of Grand Central Station. No fewer than 41 local outfitters have permits to run pack trips or hunting camps. In 1997, the last year for which figures are available, some 106,000 people visited the Teton Wilderness.

Mules loaded with gear and riders with sore behinds crowd the trails alongside the hikers. Turpin Meadow Ranch is one of the leading operators in the Thorofare. This dude ranch and outfitting business supports Dale and LaRae Castagno, plus their three sons and the sons' families.

The Castagnos are a good example of a four-generation cattle-owning family that moved into the holiday business. Mormons with their roots in Utah, the Castagnos had ranches in northern Utah and southern Idaho, but found the cattle business a struggle. When someone offered to buy their last ranch, the Castagnos agreed, but still wanted to remain stockmen if they could find a workable way of doing it. They were not successful. "I looked at over 100 ranches and every one of them was at least $1m in debt," says the patriarch Castagno. Then, in 1992, Turpin Meadow Ranch caught their eye, and the Castagnos made the transition from the cattle business to tourism.

A decade later, as the recreation market goes on growing, the Castagnos are again being bought out. The buyer plans to tear down the older buildings and build a multi-million-dollar high-end dude ranch.

The curious thing is that the Castagnos do not own one square foot of the land beneath their barns, houses and corrals. It is all leased from the Forest Service. This is a new twist on an old theme. Exploiting government-owned timber, coal and grass once brought wealth to westerners. What made the

Castagnos prosper is the draw of the Thorofare's isolation. The per-head income of Teton County, 97% of which is in effect public land, has grown 63% in the past decade, compared with an all-Wyoming figure of 9%.

How long can the idyll withstand the influx? The irony is that development restrictions, which many locals still loathe, help to pull in tourists. The Teton Wilderness forbids logging, mining and snowmobiles. This has brought, among other things, a booming trade in mountain horses and mules, which give substance to the touristy "old west" image. When that Vermont firm did its search for farthest-from-a-road places, only three spots came close to challenging the Thorofare for isolation. The trouble is, isolation no longer necessarily means peace and quiet.

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Lexington

Captain Yawn to the rescue

Aug 30th 2001
From The Economist print edition

Gray Davis is back in the frame, arguably stronger than before

PRESIDENTS come and go, but campaigning is eternal. With a mere 1,159 days until the next election, it is time to start handicapping the Democrats who want to take on George Bush in 2004. And suddenly Gray Davis, the governor of California, is back, slowly moving up the pack.

This might strike anybody who has been out of the country for the past couple of months as ridiculous. Surely not the man who plunged the Golden State into obscurity? Who became the butt of a hundred light-bulb jokes? Who became known as the Prince of Darkness? In June Mr Davis was grappling with an electricity crisis that, thanks in part to his own dithering and taste for government intervention, had already drained much of California's budget surplus and bankrupted one of its utilities. A long hot summer beckoned of rolling power cuts, industrial chaos and heat-stroke for the frail. People were talking about Mr Davis having trouble winning re-election next year.

Yet the summer disaster has not struck. The power has flowed without interruption. Firms have stayed where they are and old folk in Palm Springs have kept cool. The new power plants Mr Davis had pushed to get built have started running, and more will do so by the end of the year. Consumption has dropped—it was 12% less in June and 5% less in July than it had been a year earlier—prompted by $850m-worth of conservation efforts that Mr Bush's people scoffed at. Mr Davis has set in place new long-term contracts with power suppliers. Under pressure from Mr Davis, the federal regulator has abandoned the Bush administration's principled objections to price caps. Prices for a megawatt-hour, which averaged $320 earlier in the year and sometimes peaked above $1,000, are now capped at $92, and often run at $60.

Historians will find plenty to quibble about in Mr Davis's "great achievement". He has been lucky that the summer has been relatively mild (he might still get caught out by an autumn heatwave). His much-vaunted long-term contracts will surely prove more expensive over time than allowing retail prices to rise with wholesale prices. Price caps may well suppress the creation of new supply. His attempts to blame deregulation for a system that looked downright Soviet were bunk. There has also been a rumpus over conflicts of interest among consultants hired by Mr Davis to negotiate with the power companies.

Yet most Californians seem uninterested in the consulting scandal, let alone the finer points of energy economics. As far as they are concerned, Captain Yawn has kept the lights on and their fuel bills down. Already a terrible thought is beginning to occur to Republicans: that the whole thing could leave Mr Davis much stronger. His polling numbers have started to recover. Republican hopes that Richard Riordan, who finished off his second term as mayor of Los Angeles in July, might run against the governor seem to be ebbing away. The front-runner, Bill Jones, the secretary of state, would seem to have little chance against Mr Davis, whose campaign fund has already amassed $30m.

That money-raising power—not to mention California's 55 electoral-college votes—would automatically put Mr Davis back into contention for the White House. To this, he can add other advantages. Mr Davis is economically moderate, a Democrat in the Bill Clinton mould, but inoculated against the suspicion that California Democrats are wicked libertines by his obvious dullness, a sober family life and the military decorations he won while serving in Vietnam. He is also a better campaigner than his demeanour would suggest. During the last governor's race, he overhauled two much better-funded candidates. His patience

is legendary, though he can be ruthless when he needs to be. This week, two children of the Modesto Lothario, Congressman Gary Condit, resigned from Mr Davis's administration, after the governor finally turned on his erstwhile friend.

For Mr Bush, a revitalised Mr Davis would look a much tougher match than most of the other Democratic candidates. Al Gore (who last week dropped in on his old Silicon Valley friends to test their mood) has already lost to the president once. The other possibilities are all in the Senate, generally a less propitious starting point than a governor's mansion, and have obvious weak points—Hillary Clinton polarises people, Joe Lieberman's moment may have passed, John Kerry is a New England liberal, John Edwards is too young, Tom Daschle's skills may work better in Congress than in a national campaign.

As for Mr Davis's own weaknesses, it is hard to believe that he is not still vulnerable on the subject of energy. But that will be one subject that Mr Bush, the friend of Big Oil, the despoiler of the Arctic wilderness and the champion of nuclear energy, is unlikely to want to force to the centre of the debate. Besides, Mr Davis can claim that he saved the day in California, while Mr Bush's "national energy crisis" (which, incidentally, is no less fictitious than Mr Davis's bunk about deregulation) is far from being solved. In the spring, even while he patently had no idea what to do, Mr Davis was adept at winning the blame game.

Can Mr Davis do it? One of the rules of presidential speculation is that any campaign can be overturned by events (few predicted California's energy problems, let alone Monica Lewinsky). But in his patient, methodical way, Mr Davis will keep going, consolidating his appeal with just the sort of swing voters—Latinos, Catholics, women—that Mr Bush is trying to pull into the Republican coalition, and burnishing his CV (education reform is a possibility in California). And he will keep meeting people. A courteous man who seldom forgets a name, Mr Davis has always been hard to dislike—something that may unnerve Mr Bush. It would be galling to those (including this newspaper) who believe that Mr Davis fundamentally mishandled the energy crisis to find it turned into a source of strength for his campaign. But politics is not always fair—and the lights, so far, have stayed on.

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Mexican politics

Fox's moment of truth

Aug 30th 2001 | MEXICO CITY
From The Economist print edition

A new congressional session will be decisive for the political fortunes of Mexico's indecisive president

Get article background

THERE will be "no surprises" in Vicente Fox's first state-of-the-nation address on September 1st, say his spin doctors, bar the format: a shorter, more accessible kind of presidential speech, "so that people don't turn off the television." That just about sums up Mr Fox's presidency so far. If you picture the Institutional Revolutionary Party (PRI), which ruled for seven decades until Mr Fox took over, as a software operating system, then Mexico is still running, at best, PRI 1.1: a more user-friendly version, perhaps, but not the redesign that is needed.

Mr Fox will be inaugurating a difficult autumn session of Congress, with precious few achievements to look back on after nine months in office. His first effort was to try to end the Zapatist uprising in the south-eastern state of Chiapas, which had simmered on through the final six years of PRI rule. He pushed for, and won, congressional approval of an Indian-rights bill, demanded by the rebels as a condition for peace talks. But Congress amended the text, prompting the Zapatists to break off contact with the government.

An anti-corruption drive has been disappointing: auditors have not found the mega-crooks the public was expecting as part of the PRI's legacy, while the government has concentrated more on hunting for corrupt officials than on reducing the incentives for corruption. Other plans to increase accountability, by means of a freedom-of-information law and government performance targets, have stalled.

The biggest change has come in foreign policy. Mr Fox has improved Mexico's relations with the United States; next week, he will address its Congress during a state visit, and talk to George Bush about an unprecedented migration accord. But at home, things have moved more slowly. A tax reform, the linchpin of Mr Fox's strategy, has been delayed, both by the Chiapas brouhaha and because the government was unprepared for the opposition to its plan to increase the scope of VAT.

That delay may prove costly. The reform is needed to finance higher spending on education, infrastructure and welfare, and to strengthen Mexico's credit rating, which would open the door to more foreign capital. Standard & Poor's, one of the main American credit rating agencies, has said it will not upgrade Mexico's bonds until the tax reform is approved. Although Mexico has been largely immune to the financial woes of Argentina, it is reeling from the slowdown in the United States. After growing by 7% last year, the economy may not grow at all this year. Economists say that the recession is the price Mexico must pay for the benefits of its closer economic ties with North America. But for ordinary Mexicans, paying that price for the first time is an unpleasant shock.

Blowing in the winds

"The problem is that we basically have a populist president," says one senior official. Mr Fox wants to please many people and be open to many ideas. His cabinet contains a wide range of views. But lacking a strong programme of his own, he is apt to be blown by political winds. The overall strategy is confused; the National Development Plan, announced with great fanfare in May, was a wish-list of vague goals.

Government proposals are prone to change; for example, Mr Fox suddenly announced recently that, after all, he would not start levying VAT on books.

All this has led to tensions in Mr Fox's inner circle. His vacillations have annoyed his disciplinarian finance minister, Francisco Gil Diaz. Presidential policy advisers, supposed to co-ordinate the cabinet's work in key areas, have sometimes just caused confusion and are often ignored or bypassed. Some ministers resent Mr Gil for his fiscal rigidity. Jorge Castañeda, the dynamic foreign minister, is said to be frustrated by some of his slower colleagues; and they, in turn, detest his habit of speaking his mind on any subject that takes his fancy. "He's a blabbermouth. But he can talk all he likes, we don't pay any attention," confided one of them recently.

The next four months, though, will test the president's most difficult relationship, that with Congress. The first priority for the autumn session is the tax reform. Then there is an ambitious reform which would open much of the state-run energy sector to competition, though how is not yet clear. This is becoming increasingly urgent: the boss of Pemex, the state oil monopoly, gave warning this week that unless private investment was allowed, Mexico's oil exports could drop by two-thirds by 2006.

Mr Fox's biggest problem is that he lacks a majority in Congress. And even many congressmen from his own National Action Party are sceptical about tax reform. The PRI, the other main force, will extract a high price for its backing. Mr Fox's earlier promise of a truth commission to investigate the PRI's murky past is already on indefinite hold. The government has been in talks with PRI state governors; its best hope of getting the tax package passed is to cede some of the revenue to the states.

As for energy, any serious reform means constitutional changes, requiring a two-thirds majority. And lightening the tax burden on the state oil and electricity firms, so they can invest more, will be impossible unless the government raises more from other taxes. Until this is sorted out, it cannot decide next year's budget. The word in Congress is that all three bills will be haggled about in parallel, right up until the end of the year. The success or failure of Mr Fox's presidency may hang on the outcome of that bargaining.

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Reform in Argentina

Culling the politicians

Aug 30th 2001 | BUENOS AIRES
From The Economist print edition

The government brandishes its axe

DESPITE last month's bail-out from the IMF, Argentines face unpopular spending cuts and, after a recession lasting three years, have little love for their rulers. So it is not surprising that the latest money-saving idea involves culling politicians.

The fashion was begun by Jose Manuel de la Sota, the governor of Cordoba, Argentina's second most important province. In July, he gained popularity by holding and winning a local referendum to prune government bureaucracy. That included the abolition of the upper house in his province's legislature—coincidentally controlled by his opponents. Now President Fernando de la Rua wants to launch a similar reform. So, too, does Carlos Ruckauf, the governor of Buenos Aires.

Both men are desperate to find new ways to cut public spending. Mr de la Rua is pledged to eliminate the fiscal deficit this year; he has ordered cuts of up to 13% in government salaries and pensions. But tax revenues are falling, making the "zero deficit" target even harder to meet. Unless cuts are made elsewhere, wages might have to fall by a "socially unacceptable" 24% by the end of the year, reckons Martin Redrado of Fundacion Capital, a Buenos Aires think-tank. He hopes that this prospect will encourage reform of health and welfare spending and a reduction of bureaucracy, after years of empty promises.

The government plans to restructure several ministries and welfare agencies. Domingo Cavallo, the economy minister, has placed Armando Caro Figueroa, one of his closest aides, in charge of the tax agency, with a brief to crack down on chronic evasion. But Mr de la Rua has also announced that he wants to hold a referendum in November on slimming the political system.

Argentina's politicians are notorious for padding the payrolls of legislatures, both national and provincial, with their hangers-on. Not surprisingly, Mr de la Rua's idea has attracted flak from all the political parties, except the small force led by Mr Cavallo. But the critics have some points. Firstly, the poll will be costly, yet it would not be binding. Secondly, some of the mooted reforms, such as abolishing the (opposition-controlled) Senate, would require difficult constitutional amendments. And while provinces could manage with a single-chamber legislature, in a large, federal country there is a strong case for a Senate. The critics also dispute the government's claim that these reforms would save $1.5 billion, out of total government spending of $52 billion.

Mr de la Rua's referendum plan smacks of an effort to deflect criticism ahead of a congressional election in October, in which his weak government is likely to do badly. The more pressing task is for the president to build a political coalition capable of implementing the necessary reforms.

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Misgovernment in Paraguay

Despair and anger

Aug 30th 2001 | ASUNCION
From The Economist print edition

The impotent public rages against corruption and misery

AFTER assembling in a house in Asuncion's suburbs, a few dozen members of "Swindled Public in Action" set off in a convoy of cars to stage a noisy half-hour protest at the house of Juan Carlos Wasmosy, a former president, demanding his arrest. They blame him for the money they lost when many of Paraguay's banks collapsed in the late 1990s.

His other car's his own

Only a dozen years after democracy arrived, political disillusion in Paraguay is widespread. As their backward country of 5.5m people slides further into economic decline, Paraguayans have become fed up with a political elite they see as corrupt and complacent. Rumours swirl of a military-backed coup plot; loyal forces were put on alert when President Luis Gonzalez Macchi visited Chile last month.

But the protests have so far been ineffective. Though Mr Gonzalez has been accused of involvement (which he denies) in a $16m bank fraud, and was recently found to be driving a stolen BMW, calls for his impeachment have got nowhere. And the only popular potential replacement is Lino Oviedo, a former army chief. He led a failed coup in 1996; his supporters tried again last year. He is now under house arrest in Brazil, resisting extradition on charges relating to the murder of Paraguay's then vice-president in 1999.

"We have two types of politicians—the incapable and those capable of anything," reads a graffito on the wall of Congress. If Mr Oviedo is an example of the latter, one of the former is the vice-president, Julio Cesar Franco, of the opposition Liberals. His election last year was the first national defeat for the ruling Colorado party since the 1930s, and triggered hopes of change. But he lacks powers, has done almost nothing, and he, too, faces calls to resign.

Reformers are scattered through all three main parties, but are isolated. One such, Martin Sannemann, the Liberal governor of Central department, wants early elections (they are not due until 2003). But he admits that only pressure from the streets would achieve them, and that the protesters are as divided as the politicians.

National income per head is set to fall this year, for the fifth successive year. The government recently signed a reform pact with the IMF, promising higher taxes, lower spending and privatisation. It is unlikely to get any money until it delivers some of these promises. The government was bailed out in 1999 by loans from Taiwan. But that money is spent; in August, Paraguay's foreign minister went to Taipei seeking more.

Services such as health bear the brunt of government penury. Asuncion's Clinicas Hospital no longer has funds for antibiotics. Patients buy their own or plead with charities to provide them. A doctor on a packed ward says they are turning away cases of cerebral haemorrhage. He cheerfully admits to being a supporter of General Oviedo. That past military leaders were as corrupt as any of today's civilian politicians has been forgotten. Only the opposition of the United States, and of neighbours like Brazil, seems to stand in the way of the next coup-plotter.

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Canadian lumber

Stump war

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Canada is holding out against American pressure for managed trade in wood

NO OTHER country has more experience of the United States' abrasive approach to trade disputes than Canada, and no Canadian industry knows more about such matters than its producers of softwood lumber. But familiarity does not ease the pain: Canadian wood producers have begun to shut mills and lay-off thousands of workers in response to a decision in early August by America's Commerce Department to impose a 19% countervailing duty on timber imports.

Twice over the past two decades, Canada has cracked under such pressure, and cut deals restricting its exports. The latest deal, which expired in March, had capped duty-free exports at an annual 14.7 billion board-feet since 1996. Canada's lumber industry claims that this cost it C$700m ($480m) per year in forgone revenue, and 11,000 jobs.

At the root of the dispute lie different systems for timber rights on each side of the border. In the United States, almost all timber is privately owned and sold at auction. In Canada, provincial governments own the timber, set harvest levels, restrict the export of raw logs and set stumpage rates (or cutting fees) according to market conditions. Lobbyists for America's lumber industry claim that these stumpage rates are cheap "administratively set prices" and constitute subsidies.

The Commerce Department agreed, and went on to backdate the duty to May, claiming an unjustified inflow of Canadian wood since the agreement expired. On September 24th, the department is to rule on whether to levy additional "anti-dumping" duties that could triple the C$2 billion cost of those already in place.

This time, Canada is in militant mood. "We're not panicking and we're not rolling over," says David Gray, of the Canadian Free-Trade Lumber Council. One reason, he admits, is that half of the penalties are being passed on, through a 10% price increase, to American buyers who need Canadian wood. Another is that the federal government, the provinces and the industry have stayed united. On August 21st, Canada asked the World Trade Organisation to open consultations on the duties, which it says are illegal protectionism.

Canada's prime minister, Jean Chrétien, said he had warned George Bush that he cannot expect to restrict lumber exports while also calling for more Canadian energy. Not a threat to block energy exports, just a reminder that trade under NAFTA should be free, Mr. Chrétien said later.

On August 30th, Canadian and American officials were due to meet for their first talks under the WTO's auspices. Canada insists that this is not the first step towards a negotiated settlement. But for all the talk of economic warfare between the two close allies, diplomacy does not seem to have been entirely abandoned.

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Politics in Peru

Cleaning up

Aug 30th 2001 | LIMA
From The Economist print edition

Accusations against Alberto Fujimori and his henchmen

WITH his regime collapsing in scandal, last November Alberto Fujimori, Peru's authoritarian former president, sought asylum in Japan, whose nationality he claims by descent. Under Japanese law, its nationals cannot be extradited, so Mr Fujimori may be safe from judicial pursuit. But Japan may not be protected from embarrassment over its guest.

Hitherto, investigations into the abuses of Mr Fujimori's regime have centred on Vladimiro Montesinos, his sleazy intelligence chief, who has been imprisoned since June on some 50 charges. Investigators say they have made little progress in their efforts to link Mr Fujimori to the proceeds of Mr Montesinos's corruption, partly, they say, because they have not received much international co-operation.

But this week Peru's new, democratically elected Congress voted without dissent to endorse a report which accuses Mr Fujimori of crimes against humanity arising from two incidents in 1991-92 during the army's war against the Shining Path terrorists. In one case, an army death squad gunned down 15 people, one a child, at a charity barbecue; in the second, nine students and a teacher were abducted and killed. But even if prosecutors now charge Mr Fujimori, they may find it hard to prove that he knowingly ordered innocent civilians to be killed.

Many of Mr Fujimori's former cronies are less protected. More than 800 people are under investigation for corruption and abuse of power. Those now behind bars include the former attorney-general, the official in charge of a rigged election in 2000, and dozens of army officers. The new Congress is likely to move more swiftly than its predecessor to lift the immunity from prosecution of several of Mr Fujimori's former ministers.

The first of the many corruption cases against Mr Montesinos is likely to reach the courts soon. He has given some help to prosecutors, but has said he will deny more serious charges of trafficking in arms and drugs and human-rights abuses. Already there are rumblings from conservatives and business leaders that the investigations should cease. Some believe that the jailings have gone too far. Officials insist that the clean-up is aimed at securing justice and deterring future corruption, not at obtaining revenge. On that basis, they will start to press Japan to surrender Mr Fujimori. They may have a long wait.

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East Timor's election

On the road to independence

Aug 30th 2001 | DILI
From The Economist print edition

Questions about Fretilin's leadership

Get article background

FEW in East Timor have doubts about which party will win the election on August 30th. The question is, by how much? Fretilin, otherwise the Revolutionary Front for an Independent East Timor, has changed somewhat since the heady days of 1975, when it won a brief civil war in the former Portuguese colony and East Timor was declared independent, only to be faced nine days later with an Indonesian invasion. Fretilin has toned down its left-wing talk and abandoned its Marxist leanings. It has run a slick campaign to try to win the favour of some 400,000 voters and predicts it will take 80-85% of the 88 seats in the assembly. That would allow it to dictate the country's constitution, the assembly's first task, paving the way for a presidential election and independence next year. At present East Timor is run by a United Nations administration.

Fretilin's chairman, Lu-Olo, and its secretary-general, Mari Alkatiri, insist that it will produce a sensible constitution, guaranteeing freedom of speech and association, and the right to a job. But some doubts remain. Mr Alkatiri spent nearly all the years of the Indonesian occupation in Mozambique, another former Portuguese colony, working with Frelimo, a Marxist group. He strongly defends his Frelimo adventures. Mr Lu-Olo, real name Francisco Guterres, a guerrilla commander in East Timor under the popular Xanana Gusmao, is seen as more moderate than Mr Alkatiri. Fretilin harks back to the nine-day government of 1975, which it wants formally to restore. Not all Timorese recall this episode with enthusiasm. Fretilin killed many people in its struggle for power, they say, and has not apologised.

In recent weeks, a new force has emerged in Timorese politics, largely on the back of dissatisfaction with Fretilin. The Democratic Party is led by Fernando de Araujo, who spent six-and-a-half years as a political prisoner in Jakarta's Cipinang jail with Mr Gusmao. He was released in 1998. His party has come from nowhere to look a likely runner-up.

The party has attracted strong support from the young, from intellectuals and from the former clandestine network that slowly undermined Indonesian rule in East Timor while Mr Alkatiri was in Mozambique. Mr de Araujo accuses Fretilin of intimidation in the election and has compared its tactics to those of the Indonesian-backed militias in 1999, when East Timor overwhelmingly voted for independence in a UN-run referendum. The Democratic Party would like to see independence day as August 30th, the date of the referendum, not November 28th, the date the nine-day republic was founded in 1975. A natural ally of the Democratic Party is the Social Democratic Party, a possible third force among the 16 parties contesting the election. Its leader, Mario Carrascalao, was governor of East Timor for ten years during the Indonesian occupation. Timorese did not consider him a collaborator. He did his best for his fellow countrymen, and maintained secret links with Mr Gusmao.

The UN's head of state in East Timor, Sergio Vieira de Mello, says he does not believe there is any policy of intimidation by Fretilin. Many Timorese say the UN is being hoodwinked and is too close to Fretilin.

Fretilin's relationship with Mr Gusmao is somewhat clouded. Mr Gusmao, a poet and a reluctant politician, left Fretilin in the late 1980s. He has finally caved in to public pressure and said he would run for the presidency if the political parties wanted him to. Several have already nominated him, including Fretilin and the Democratic Party. He would probably be unbeatable.

But without naming names, Mr Gusmao says certain parties have nominated him only in response to popular pressure. Those close to him say his relations with Fretilin these days are not good and he would be unlikely to work well with Mr Alkatiri. Fretilin has suggested a system of government in which the president would have some key powers, but a prime minister would run most internal affairs. Such a system would sharply reduce Mr Gusmao's power over the first government, were he to become president.

Despite claims of intimidation, the campaign has been fairly free of violence. The turnout on polling day was expected to be huge. Timorese put on their best clothes and formed long queues outside voting stations. The result of the election will probably be known by September 7th, and be made official on September 10th. The UN administration of East Timor, with its well-paid jobs that have been criticised by some Timorese, is due to end next year. The UN's chief electoral officer, Carlos Valenzuela, says the aim has been to produce an election which the Timorese can later repeat, at a time when they will be entrusted to conduct their own affairs without the UN as their protector.

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Mobility in China

Off to the city

Aug 30th 2001 | BEIJING
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Government eases the rules

IT WAS one of Mao Zedong's many big ideas, and thus far one of his most enduring. In the late 1950s, at the time of the "great leap forward", China established its *hukou*, or household registration system, which required people to live and work only where they were officially permitted to. For a government intent on running its economy according to a strict central plan, it was well to have people stay where they were told. For China's hundreds of millions of rural dwellers it made leaving their village nearly as difficult as leaving the country.

AP

Now to move in

Over the past 20 years China has moved steadily further from central planning, and workers have moved in huge numbers away from the nation's economically backward countryside to its far more vibrant cities. According to official estimates, China's migrant labour force now numbers somewhere around 100m. The government expects another 46m to come looking for jobs in the cities in the next five years as the number of surplus rural workers swells to 150m.

In light of such numbers, China's announcement on August 16th that it plans to revamp the registration system seems a bit like closing the barn door after the horse has escaped. But if the government carries through with its plan to abolish restrictions on labour mobility, it will in fact make a huge difference to the lives of those migrants.

Many of today's migrant labourers still find it exhausting to get permission to move. They can spend months upon months of their time chasing—and paying for—the dozen or so certificates and approvals needed to live and work legally under the *hukou* system. By the time they get the last of the necessary documents, the first may have lapsed. At the end of it all, they have only temporary and limited residence privileges. Not surprisingly, some migrants choose to take jobs on building sites or handling rubbish with no documentation at all. They earn far less than legal workers, and are vulnerable to mistreatment if they get caught by the police.

Now, according to China's powerful State Development and Planning Commission, the government is working on a plan that will do away with migration restrictions over the next five years and create a unified national labour market. The newly liberated workers will be able to contribute to a pension fund wherever they are, and carry their benefits from place to place. On August 27th the Ministry of Public Security, the main administrator of the *hukou* system, confirmed its support for the reforms. The old system, the authorities say, put "excessive restraints" on mobility and hindered the distribution of labour according to market demand.

While that is clearly true, it has also helped avert an outcome that many of China's urban dwellers dread: an unrestrained influx into the cities of people from the countryside. While city people are glad to have enough migrants to handle the jobs they themselves do not want, they fear that too many will put unbearable strain on housing, communications and other resources. Some municipal governments have already tinkered with existing rules to admit only "desirable" outsiders. The cities of Shenzhen and Zhuhai offer residency to those who can buy property, and Beijing grants documentation to technical workers with senior qualifications. In light of such distinctions, Anita Chan of the Australian National University's China and Korea Centre has likened the *hukou* system to South Africa's apartheid. While the discrimination in China is not racial, she notes that "the underlying economic logic of the system" has

been based on similar mechanisms of regulating the supply of cheap labour and abusing the rights of migrants.

Miss Chan wonders whether restrictions will in fact be abolished on equal terms for skilled and unskilled workers. In the private view of one Chinese sociologist in a government think-tank, the answer is clear. Regardless of what the authorities say, China's largest cities will never allow in unrestricted numbers of rural dwellers. "Everyone knows that there would be utter chaos if there were really no restrictions. And that will never be allowed to happen."

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AIDS in China

Confession time

Aug 30th 2001 | BEIJING
From The Economist print edition

"A very serious epidemic"

Get article background

Singer Sun Yue gives blood safely

AFTER failing for months, if not years, to come publicly to grips with a fast-growing problem of HIV and AIDS, Chinese health officials on August 23rd pulled their heads out of the sand, at least partially. Talking to reporters in Beijing, the vice-minister of health, Yin Dakui, acknowledged that China is "facing a very serious epidemic" and admitted that negligence by provincial and local-level officials had contributed to the spread of the disease.

This comes as no news to the health professionals, Chinese and foreign alike, who have been trying for years to study the problem despite official stonewalling. And it certainly is not news to the tens of thousands of people, possibly more, in Henan province who have been infected by selling their blood at $5 a go to shoddy collection centres using shared and unsterilised equipment.

According to Mr Yin, China had 600,000 people infected with HIV, which can lead to AIDS, at the end of last year, but he predicted that the country would meet its goal of keeping the number below 1.5m by 2010. However he also said that the number of infections reported had risen by 67% during the first six months of this year, compared with the same period last year. That trend, together with others, such as a rising percentage of HIV-positive drug users, will make it difficult for China to meet its target, according to other experts.

A recent report by the United Nations' AIDS office put the number of HIV sufferers in China at over 1m at the end of 2000, and predicted, far more gloomily, that the country might by 2010 have 20m victims to deal with. However overdue it may be, the high-level official attention given to the matter marks a vital turning point in China's struggle to deal with not only the spread of HIV, but also the interference of provincial officials in Henan, one of the country's hardest-hit areas.

Beginning in the late 1980s, several rural counties in Henan had turned blood collection into something of an industry. Lacking other sources of income, many residents sold blood on a regular basis to government or army-run collection stations that failed to follow basic guidelines for sterilisation. As the virus spread, local officials tried to cover up the problem. Journalists and central-government investigators were kept out, and sometimes threatened with violence if they persisted. Community workers and AIDS sufferers who tried to get outside help ended up earning much attention from the police, and little from health agencies.

Attention now from Beijing will not include enough money to pay for the expensive life-prolonging medications that are available, but Mr Yin announced a plan to spend $23m on education programmes and on efforts to clean up the nation's blood-collection system.

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Taiwan and China

Not so strait

Aug 30th 2001 | TAIPEI
From The Economist print edition

An economic rebuff from Beijing

THE Taiwanese have not seen a contraction of their economy since they began compiling records in 1952. Two generations have grown up taking 8% annual growth for granted and thinking recession was an ailment of the sclerotic West. So with even the usually optimistic government number-cruncher predicting growth of minus 0.3% this year, the mood is close to panic. That may help explain a new readiness to contemplate expanding economic ties with mainland China.

The country over-depends on exports of information technology to the United States. A fall of some 30% in American orders for electronic goods in the first half of this year has caused pain in Taiwan, where many of these products are made. A conference called by the president and involving business leaders aimed to resurrect the economy. It was proposed to abolish restrictions on investment and other business activities across the Taiwan Strait, open Taiwan's property and equities markets to Chinese capital and, perhaps most importantly, end a 51-year-old ban on direct commerce, communication and transport across the strait. At present nearly a quarter of Taiwan's exports go to China, mostly semi-finished products completed in China and re-exported, but there is little moving the other way.

Businessmen see Taiwan as a centre for servicing the industrial hinterland along China's eastern coast just as, in the 1980s, Hong Kong became a service centre for the next-door province of Guangdong. This would diversify Taiwan's economy away from its double dependence on manufacturing and the United States. The government, which agreed in advance to implement whatever the conference proposed, finds itself committed to the biggest change in its relations with China since its forerunner fled to Taiwan after the Communist revolution of 1949.

Implementing the policy changes is not, however, entirely up to Taiwan. Direct trade, postal and transport links cannot be opened without discussions with China, and here the prospects are not good. For nearly six years China has refused to have any talks with Taiwan unless the island acknowledges a "one China" policy. What this is depends on China's mood. Sometimes it entails an acknowledgement that Taiwan is a province of China, at other times it means simply expressing a commitment to eventual reunification.

China has watched Taiwan's economic problems with glee. Once the Taiwanese understand that China controls their economic well-being, it is argued, they will seek political integration. Currently China's mood is hostile. On August 29th the government said through its official news agency that it ruled out direct trade links with Taiwan unless the island embraced the principle of "one China", whatever that may mean at the moment.

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Fiji's future

Instead of rebellion

Aug 30th 2001 | SUVA
From The Economist print edition

A need for stability

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A GENERAL election in Fiji is an unhurried affair. Voting started on August 25th and has continued all this week. It will take a little while to collect the ballot boxes from Fiji's 110 populated islands, and counting is not likely to start until September 3rd. The final result is expected four days later, although this may be an optimistic prediction.

The people of Fiji, though, have much to talk about as they await the outcome. How, for example, is George Speight likely to fare? He was the leader of a rebellion last year that forced the country's elected government out of office, and is on trial for high treason. He acknowledges his part in the rebellion but claims that the army gave him immunity for freeing his prisoners. Before voting began, his trial was adjourned until next year. From his prison cell Mr Speight is standing for election under his Fijian name, Ilikini Naitani, in his home area of northern Tailevu.

If he wins a seat, he may try to have the treason charge lifted. If the charge stays and he is convicted, he will have to give up his seat. Mr Speight is likely to have the support of indigenous Fijians who want to stop Fijians of Indian descent from holding political office, the rallying cry of last year's rebellion. His supporters have founded a new political party, the Matanitu Vanua (Confederacy of the Indigenous Peoples), otherwise quaintly known as the Conservative Alliance. Most of the party's candidates in the election were implicated in the rebellion. The party wants the constitution to be changed to allow the country's 52% Fijian population to have permanent political control.

In a constituency on the western side of Fiji's main island, Viti Levu, Mahendra Chaudhry hopes to retain his seat. Mr Chaudhry, the country's first Fijian of Indian descent to become prime minister, was held prisoner with many of his cabinet ministers until the rebellion collapsed. His political support among the 44% of the population who are of Indian descent remains strong. His constituency is in the heart of Fiji's sugar plantations, where Indian farmers have for generations cut cane on land leased from indigenous Fijians.

The present prime minister, Laisenia Qarase, was installed by the army after the rebellion as the head of an interim government. His party aims to provide a moderate ethnic Fijian alternative to Mr Chaudhry's Labour Party. However, with 18 parties and 351 candidates competing for the 71 seats in parliament, it is unlikely that any party will gain an outright majority. If the election instead produces two racially defined groups, one backing Mr Chaudhry and the other centred around indigenous Fijian extremists, the country is unlikely to end up with the stable multi-ethnic government it needs.

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Pressures on South Korea

A president in a hurry

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From The Economist print edition

Fall in popular support

THE popularity of Kim Dae Jung, South Korea's president, as measured by opinion polls, is now only 20%, down from a high not long ago of 80%. Yet by some measures he has been a successful president. South Korea has repaid $19.6 billion borrowed from the IMF during the financial crisis in 1997, an accomplishment celebrated at a concert in Seoul on August 26th, which Mr Kim attended. It still has to repay $10.7 billion borrowed from the World Bank and the Asian Development Bank, but should have no problem doing so. Its foreign-exchange reserves have been built up to a healthy $97.8 billion. Mr Kim is given much credit for this.

South Korean newspapers have been critical of the president since 23 media groups have received demands for a total of 506 billion won ($400m) in back taxes. The owners of three daily newspapers have been accused of tax evasion and embezzlement. But claims that press freedom is at stake do not seem to convince ordinary Koreans. The tax demands are accepted as lawful.

What has turned many Koreans against their president is that they feel he is trying to do too much too quickly, and with limited results. A law passed last year prevents doctors from selling prescribed drugs directly to patients, and pharmacists from selling drugs without a prescription from a doctor. The government thought this would reduce the cost of the national health-insurance fund. In fact doctors have since been prescribing large quantities of drugs, especially antibiotics. The fund almost ran out of money and had to be topped up with about $1 billion from the government.

Financial and corporate restructuring has been costly but incomplete. The government has spent more than $90 billion to restore the financial system. But banks are still saddled with bad assets; three out of ten manufacturing firms surveyed by the central bank are failing to generate enough cash to pay interest on their debts. Big companies that went bankrupt continue to stay in business, kept afloat by state-owned banks. The government is due to introduce a new law on September 14th to expedite corporate restructuring, but whether it will apply to those big firms is unclear. Real GDP is forecast to grow by about 3% compared with last year's 8.6%. There has been a sharp decline in exports of goods and services, which accounted for 52% of GDP last year.

Then there is North Korea. Mr Kim's minority government is under pressure to sack Lim Dong Won, the unification minister. Mr Lim is the architect of Mr Kim's sunshine policy of engaging North Korea by providing unconditional aid to the impoverished country where the rulers enjoy a lavish lifestyle and even import chefs from Italy to make pizza. The sunshine has become cloudy over North Korea, which has refused official contacts with the South since March. But Mr Kim seems determined to keep the policy and its architect, whatever the opinion polls say.

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Sri Lankan politics

No reconciliation

Aug 30th 2001
From The Economist print edition

Party talks fail

UNTIL recently tourists did not feel in danger in Sri Lanka. Although a civil war was being fought in the north-east of the island, where Tamil Tigers demand a separate state, the sounds of battle never reached the splendid beaches of the south. It was a good place for anyone in the grey northern countries to seek the sun relatively cheaply. The goodness ended on July 24th when the Tigers shot up Colombo's airport, Sri Lanka's main gateway for visitors, an attack that left 18 people dead and destroyed a dozen aircraft.

Insurers have declared the entire island a war zone. Hotels in Colombo, now less than 10% occupied, are laying off staff. The clothing industry, a big exporter, fears that the foreign companies that dominate the business may move their factories to safer locations in the subcontinent.

The best thing to say about Sri Lanka is that after 18 years of war the country remains a democracy. But the politics of the place look dismal. Chandrika Kumaratunga, Sri Lanka's executive president, who was elected partly on a promise to end the civil war, has seen one more peace effort fail. The government proposed this week a ceasefire linked to new talks with the Tigers but Sri Lankans received the news without optimism. The well-meaning Norwegians, hailed as peace brokers, appear to have retired bruised.

This week, in what seemed a desperate move to try to bring some direction to the country's affairs, Mrs Kumaratunga's ruling coalition, the People's Alliance, had discussions with the United National Party, the main opposition party in parliament, with a view to setting up a government of "national reconciliation". The talks ended inconclusively. The government faces a rough time when parliament reconvenes on September 7th. The opposition is seeking to impeach Sarath Silva, the chief justice of the Supreme Court, accused of 14 acts of misbehaviour, including living with a woman not his wife.

Meanwhile, the government has been warned by its intelligence people that the Tigers are preparing to have another try at retaking Jaffna town, which was once their stronghold, but is now under government control. The Tigers are said to be well equipped. But so are the government forces, which have been revamped with help from Israeli advisers. The one prediction that can be made about any future battle is that it will be a bloody affair.

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Israeli-Palestinian fighting

The tanks of August

Aug 30th 2001 | BEIT JALA AND JERUSALEM
From The Economist print edition

The storming of Beit Jala has darkened the mood in Israel as well as inflamed the feelings of Palestinians

Get article background

IN THE past week Ariel Sharon, Israel's leader, has turned up the heat of the Palestinian *intifada* by several degrees. On August 27th, Israeli helicopters hovering over Ramallah killed Mustafa Zibri (better known as Abu Ali Mustafa), the leader of the Popular Front for the Liberation of Palestine (PFLP), a radical faction of the Palestine Liberation Organisation. That night, Israeli tanks rolled into the Palestinian village of Beit Jala. Palestinian gunmen had been using the village as a base to fire on Gilo, a Jewish settlement built on land in occupied East Jerusalem.

The army said it would stay put until Palestinian guns were "silenced". The Palestinians said they would not stop firing until the Israelis left and, to show earnest, fired five or six mortar rounds into the heart of Gilo and peppered it with small-arms fire. On August 29th—after pressure from the European Union, the Palestinians said—the two sides agreed to stop shooting and start withdrawing simultaneously. Despite a last massive blast of Palestinian gunfire, Israel took its forces out the next morning. Would they return if the firing resumed? "Absolutely", said Binyamin Ben-Eliezer, Israel's defence minister.

Israel had not gone into Beit Jala lightly. The incursion came after months of hesitation in Mr Sharon's cabinet, and its failure to stop Palestinian attacks has darkened the country's mood. Although Gilo, a sprawling community of 45,000 people, is built on occupied territory, Israelis consider it part of Israel's capital. Mortar shells falling on Gilo arouse very different reactions among ordinary Israelis than mortar shells falling on the Jewish settlements inside the Gaza Strip, where they land almost nightly. Those fired on August 28th reached the centre of the suburb; one landed on an empty kindergarten. The new school term starts next week, and it would be hugely embarrassing for the government if the schools in Gilo stayed closed.

The position of Shimon Peres, as the senior Labour Party figure in the national unity government and the major force for restraint, has now been seriously compromised. He has let it be known that he was not consulted over the assassination of Mr Zibri, nor over Beit Jala. "How shall I show my face in the world?" he sighed as he wearily set about soliciting friendly governments to put pressure on Yasser Arafat, the Palestinian leader. Mr Sharon's aides say both decisions were adopted in principle some time ago, and that Mr Peres was on board. Their specific timing had been left to the prime minister and the minister of defence, another Labour man.

Mr Peres is not explicitly threatening to quit the government. Even if Labour did walk out, Mr Sharon would retain a comfortable majority now that the Centre Party, with its five Knesset seats, has joined his coalition. On September 4th, Labour's 117,000 registered members are to elect a new leader. The post has been vacant since Ehud Barak resigned after his crushing election defeat in February by Mr Sharon. Mr Ben-Eliezer is running against the more doveish Avraham Burg, the speaker of the Knesset, whom the polls put slightly ahead. The race has aroused little interest, partly because members believe that, whoever wins, Mr Peres will remain the party's real policymaker in the immediate future. In the longer term, some Labourites expect Mr Barak to make a comeback before the next general election. Mr Burg says that, as leader, he would "reassess" Labour's role in the unity government. But he knows that the party is loth to move to opposition.

Mr Peres, in particular, is reluctant to leave Mr Sharon to his own devices, especially when those are becoming increasingly brutal. Mr Sharon's logic is clear: he means to threaten the existence of the Palestinian Authority until Mr Arafat gets the message, calls off the *intifada*, arrests the gunmen and accepts a ceasefire on Israel's terms. The Palestinian consensus is that Mr Arafat can take none of these steps without risking a revolt against his regime, including one by his own Fatah colleagues.

The killing of Mr Zibri has strengthened this view. He was not only the most senior Palestinian killed by Israel in the *intifada*, but perhaps the most important Palestinian political leader to be killed since Israeli commandos gunned down Mr Arafat's deputy in the PLO, Khalil Wazir (Abu Jihad), in Tunis in 1988. Israel insists that Mr Zibri was directly involved in a string of car bombings in Jerusalem, as well as in dozens of armed attacks in the West Bank.

Palestinians (unaware that the decision had been long planned in Israel's cabinet) see his murder as straight revenge. The assassination came after a weekend in which seven Israelis were killed, including three soldiers at a heavily fortified military base in Gaza. Responsibility was claimed by the leftist Democratic Front for the Liberation of Palestine, but the assault was carried out by two men belonging to Mr Arafat's Fatah movement, who prepared for their deaths with all the religious ceremony of Hamas suicide bombers. The same unity of the factions was seen in the response to Mr Zibri's murder. Thousands of Palestinians took noisily to the streets not only in Gaza and the West Bank, but also in neighbouring countries such as Jordan, Lebanon and Syria, where the PFLP still commands considerable support.

Mr Arafat, his aides say, is still committed to the ceasefire drawn up by the Mitchell Commission in May. But he wants some form of international intervention to ensure that Israel will withdraw from Palestinian civilian areas, freeze all building of settlements and resume political negotiations. The entanglement of both the EU and the United States in Beit Jala is precisely what he wishes to see. If the ceasefire unravels he is ready to let the ground crackle and burn, and not only in the occupied territories.

Mr Peres says he hopes to talk to Mr Arafat some time next week. But on September 13th Mr Arafat is scheduled to be in Damascus, the latest phase in the slow rapprochement with Syria's president, Bashar Assad, that began when the two men met and exchanged cordial words at an Arab summit in March. Eight years ago to the day the Palestinian leader was in Washington, signing the Oslo accords, shaking Yitzak Rabin's hand and embracing President Clinton. Mr Arafat's message is plain: times change and so, if necessary, will my allies.

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The world's food

Feast or famine?

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Prognostications for the next 20 years

THE world's population is forecast to reach 7.5 billion by 2020, and growing prosperity, especially in China, is fuelling a rising appetite for meat and cereals. Yet it is becoming harder to find new farmland, water is increasingly scarce and crop-yield growth is slowing. Already, 167m children are malnourished. Are hungry times ahead?

Not necessarily, according to a new study published by the International Food Policy Research Institute, a food-policy think-tank. The study projects food supply and demand, trade and prices from 1997 to 2020 for 36 countries and 16 commodities. If current trends hold, the report sees cereal consumption rising by more than 33% and meat consumption by 57%. But only 9% more land will be used for cereal production in the developing world, and the average annual growth in cereal yields worldwide will fall by more than a third compared with rates in the 1980s and 1990s. More trade between rich and poor countries would help, but not if subsidies and other "trade distortions" persist. Sub-Saharan Africa—battered by AIDS, civil war and political mismanagement—will have a hard time simply standing still.

Yet if developing countries were to increase their investment in factors that affect food security—from agricultural research to rural roads to education—by more than a third over present rates, to $802 billion between 1997 and 2020, then the study predicts that agricultural yields will rise, prices will fall and the number of malnourished children will tumble to 94m. A big if.

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Nigeria

Never apologise, never explain

Aug 30th 2001 | ABUJA
From The Economist print edition

A commission has been set up to look into past misdeeds. The generals who are guilty of them do not want to attend

Get article background

Justice Oputa investigates

ON A leafy hill-top overlooking the northern Nigerian town of Minna stand two splendid back-to-back mansions. They belong to two childhood friends, Ibrahim Babangida and Abdulsalami Abubakar, who, as wealthy generals, ruled Nigeria from 1985 until an election in 1999. They acquired most of their wealth in the years they were in power.

Yet peaceful retirement is not in prospect. Their names, and that of Muhammadu Buhari, another former military head of state, have been persistently mentioned in a series of public hearings into three decades of murky events in Nigeria. The dirt has been aired on national television, and now the press wants to see the men in court. On September 3rd, after an August break, the human-rights panel that is conducting the hearings will resume its work, and the generals have been politely requested to appear.

Around the world, more and more serving or former leaders are being called to account for their past actions. Could it happen in Nigeria, too? President Olusegun Obasanjo says he hopes so. Mr Obasanjo, himself a former military ruler, set up the human-rights panel two years ago. It has seven members, including a much-respected former Supreme Court justice, Chukwudifu Oputa, who heads it, and Matthew Kukah, a Catholic priest. The panel is supposed to do for Nigeria what the Truth and Reconciliation Commission did for South Africa. Mr Obasanjo has even been called before the panel himself. On September 11th he is due to appear to answer questions about the death in 1977, after an army raid which he had ordered, of the mother of Fela Kuti, Nigeria's best-known musician.

Hearings began last October in the capital, Abuja, and have continued in the main cities of Lagos, Port Harcourt, Enugu and Kano. About 11,000 depositions have been taken, on subjects ranging from the pogroms carried out in northern Nigeria against the ethnic Ibo before the civil war of 1967-70, to the assassinations and torture of opposition leaders in the mid-1990s. Yet the signs are that not much truth has yet been aired or reconciliation achieved.

On the Ibo pogroms, the political leaders of the two groups involved have merely traded insults and accusations. On the subject of the execution of Ken Saro-Wiwa, a campaigner for minority rights, the head of the task-force responsible for oppressing Mr Saro-Wiwa's people, the Ogoni, said bluntly that he would do it all again, despite more than 8,000 depositions by Ogoni before the panel. So far, no important Nigerian has been prosecuted except the son of the late military ruler, Sani Abacha, and two of his father's henchmen.

The three generals, too, have so far refused to appear—or have indicated that they will do so only if strict conditions, such as the ruling-out of embarrassing questions, are agreed in advance. The panel is not a court of law, but it hears its witnesses under oath. If Mr Buhari were to appear, he could be asked, for example, about the bungled attempt in 1984 to kidnap a dubious Nigerian politician, Umaru Dikko, who was found bound in a crate at London's Heathrow airport.

Mr Abubakar, who ran Nigeria for just 11 months in 1998 and 1999, could be expected to face questions over the mysterious deaths of both his predecessor Abacha, and a jailed civilian opposition leader, Moshood Abiola. Both deaths occurred within less than a month, between June and July 1998. Mr

Babangida, who ran Nigeria from 1985 to 1993—and who is still both immensely wealthy and politically influential—could be questioned about the killing in 1986 of a leading journalist, Dele Giwa, then editor-in-chief of *Newswatch*, and about the annulment by the armed forces of the 1993 presidential elections apparently won by Mr Abiola.

Messrs Babangida and Abubakar are especially eager not to be asked to account for the reported disappearance of more than $12 billion in public funds while they were in charge. Lawyers acting for the panel should not be allowed to ask about “just anything”, a lawyer for Mr Babangida told reporters in mid-August. Maintaining the dignity of his client was “immensely important”, he said. Apparently rattled, Mr Babangida on August 17th cancelled, at the last minute, the planned celebrations for his birthday and flew off to Saudi Arabia instead.

Hopes that the wrongdoers might get their just deserts were raised by the publication, in July, of two reports from a series of inquiries into past regimes. Such inquiries have been held before, but their findings have often been hushed up or binned. The reports name 52 prominent and wealthy Nigerians who allegedly stole land and property from the government. Yet it is not clear that anything more will be done about them.

That is the situation in which the panel, too, finds itself. Justice Oputa has the power to order the arrest of those who refuse a summons; but he is a diplomatic man, and less keen to use that power than some other members of the panel. If he dares to exercise it, and gets the generals on the stand, Nigerians will certainly be interested to hear how they excuse themselves. If he fails either to bring them in or to prosecute them, Nigerians will suspect that the chief purpose of the panel is to embarrass Mr Obasanjo’s political rivals.

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Race in South Africa

When dogs don't bark

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As South Africa plays host to the third UN conference on racism, how much progress has it made itself?

UNLIKE people, a dog that is a racist cannot hide the fact. Your correspondent's dog, without any encouragement from past owners, barks ferociously at black people but merely slobbers at whites. Ingozi—the name means "danger" in Zulu—guards a house in a wealthy, mostly white, suburb of Johannesburg. In common with many South African dogs, he has inherited the assumption that any approaching blacks may be robbers.

AP

Not equal yet

Ingozi's instincts are a reminder that old racial animosities still fester in South Africa beneath a brighter surface. In many ways, since the first all-race elections in 1994, the country has made a remarkable transformation from the world's most openly racist society into a tolerant and democratic one. These days, instead of waving the old (apartheid) South African flag, Afrikaners at rugby matches paint the rainbow flag on their faces. A new black elite mingles with other races in Johannesburg's malls and restaurants. Television dramas, comedy shows and newspaper cartoons all dare to poke fun at race relations, a sign of a society now a lot more at ease with itself.

South Africa's political transformation is even more obvious. The once all-white parliament is now multi-hued and dominated by the party of black liberation, the African National Congress (ANC). The 1996 constitution celebrates a country "united in our diversity" and recognises the "injustices of our past". It goes on to recognise 11 official languages and to affirm equality before the law for all South Africans. It outlaws discrimination on grounds of race, sex, sexual orientation, disability and so on. It makes an exception, however, for laws aimed at uplifting "categories of persons" discriminated against in the past. A series of laws has been passed obliging government and business to discriminate in favour of blacks, women and others disadvantaged by apartheid.

All the main political parties support South Africa's multiracial democracy. But scratch the surface, and racial division reappears. The ANC is largely black and dominated by Xhosas; the Democratic Alliance is backed mainly by whites and coloureds; the Inkatha Freedom Party is Zulu; the Freedom Front is white and Afrikaans-speaking. Parliamentary debates are tainted by racial mud-slinging. The ANC accuses critics of racism; they retort that the ANC too often blames the racist past for its own failures.

At first glance, ordinary folk do not seem to share their obsession. "Fewer than 5% of South Africans spontaneously identify racism as a problem," says Anthea Jeffery, a consultant at the South African Institute of Race Relations (SAIRR). Crime, housing and jobs matter more. But these issues are racial too. Whites who complain about crime are usually referring to black-on-white crime, and sometimes by extension to the new South Africa. Blacks who lament their poverty are keenly aware that their former oppressors are rich.

The government's efforts to create a black middle class have seen some limited success. After 1994, there was a surge in black-owned companies' share of the market capitalisation of the Johannesburg Stock Exchange, though it slumped recently to only 2% of the total (more if you define black ownership more loosely), according to BusinessMap, a consultancy. With government help, blacks have made their mark in mining, media and telecommunications. Prominent businessmen such as Cyril Ramaphosa, Saki Macozoma and Tokyo Sexwale serve as role models for young blacks. But all three are former ANC heavyweights. Not many well-known black entrepreneurs have succeeded without political clout. Many

have done no more than use their connections to persuade banks to lend them money to buy portions of existing white-owned businesses. That is hardly an example that ordinary blacks can copy.

Now that white-owned businesses are no longer forced to exclude blacks, they seem to be putting profits before prejudice. A local newspaper recently sent a black reporter and a white one to see whether restaurants in Johannesburg treated them differently, but found no evidence of discrimination. This does not mean that none of the waiters or managers was racist, merely that businesses, left to their own devices, have a strong incentive not to alienate paying customers.

Habits hard to break

Apartheid is no longer the law, but blacks and whites still live largely separate and unequal lives. Crowds at rugby games are still almost exclusively white, at football matches almostly entirely black. Even in the most youthful, trendy and relaxed parts of town, there are very few mixed-race couples. Economic segregation keeps people apart. Johannesburg, South Africa's most mixed city, is divided into the expensive (and mainly white) northern suburbs and separate poor districts which are almost entirely black.

Small extremist parties survive, and could cause trouble. The Pan Africanist Congress, for example (whose slogan used to be "one settler, one bullet"), encourages landless supporters to invade private property. The invasions have not so far been widespread or violent, as in Zimbabwe, and the government has evicted many squatters. But white farmers are more likely to be killed than almost any other group in society: 274 are killed for every 100,000 people each year. The Freedom Front, a right-wing party of Afrikaners, claims that some of the murders are political, the long-expected revenge that many whites have feared. "They will never forgive us for what we have done," confides one white woman.

Some believe that too few South Africans are making personal efforts to take responsibility for the past. Nkosinathi Biko, the son of Steve Biko, a writer and political activist murdered by police in 1977, says that too many people, especially whites, expected the much-vaunted Truth and Reconciliation Commission (TRC) to do that job for them. The blacks who suffered, he thinks, have largely forgiven their oppressors, but the whites are still sour.

Opinion polls bear him out. A study in June of nearly 4,000 people by the Institute for Justice and Reconciliation, based in Cape Town, found that 76% of black respondents believed the TRC had done a good job, but only 37% of whites agreed. Some 72% approved of amnesties for crimes committed under apartheid, while only 39% of whites did. But over half of all blacks thought whites untrustworthy, half found it hard to imagine having a white friend (only a fifth said that they had ever eaten a meal with a white person), and roughly a fifth thought the country would be better off without whites.

Prosperity could perhaps ease South Africa's racial tensions. But average incomes have barely grown since 1994, and the gap between whites and blacks remains huge. Poor blacks have stayed poor: an estimated 40% are unemployed, compared with 7% for whites. Although black wages have edged closer to white wages since the 1970s, they remain far lower. According to the University of South Africa, the combined income of black South Africans (who make up 78% of the population), will surpass that of whites (10.5%) for the first time only this year.

Against this background, white complaints about positive discrimination can sound ridiculous. But they should not be discounted. The most likely South Africans to emigrate are the young, white and skilled. Their departure applies a brake to economic growth, which makes it more likely that poor blacks will stay that way.

Positive discrimination is also partly to blame for the general rise in unemployment since 1994. Employers above a certain size are obliged to submit annual reports to the government on their progress towards making their workforces three-quarters black at all levels, from the shopfloor to the boardroom. If sued for racial discrimination, the onus is on them to prove their innocence. That a black applicant was unqualified is no defence; employers must demonstrate that he or she could not have acquired the necessary skills in a reasonable time. Faced with such obligations, firms tie themselves in knots to avoid hiring anyone at all.

Racism begins at home

On top of all this, there are signs that a new racism is emerging. Black South Africans are increasingly resentful of Africans from other parts of the continent. Lax immigration policies, and a border of roughly 3,000km (2,000 miles) shared with six other countries, have allowed large numbers of Africans from north of the Limpopo river to move in. Mozambican immigrants are sometimes blamed for bringing AIDS to South Africa, and Nigerians for bringing drugs and crime to its cities. In September 1998, two Mozambicans and a Senegalese were killed on a train outside Pretoria by a mob angry at foreigners "taking jobs away" from South Africans. Television footage of white policemen setting their dogs on terrified illegal immigrants last December provoked outrage, but also drew comments (from the president, Thabo Mbeki, for example) that racism is deeply entrenched in the country.

Yet, for all the pessimism, it is worth taking the long view. As Aziz Pahad, the deputy foreign minister, puts it, "Racism can't deepen here after 300 years. It can't go worse than before." In the 1980s, many predicted a race war in South Africa. It never happened, and it is extremely unlikely in the future, not least because most of those who do not like the new South Africa can pack their bags and fly out.

In the end, South Africa will shake off apartheid only if enough individuals do their bit to foster good relations between the races. In rural areas, some have launched "consumer campaigns" to promote shops and other businesses as anti-racist places. Such small-scale activities, along with laws against discrimination and sound macro-economic policies, should push South Africa's transition further and faster. Johannesburg's dog-owners could do their bit, too.

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Germany

Will the economy—and Gerhard Schröder—bounce back?

Aug 30th 2001 | BERLIN
From The Economist print edition

Germany's ebullient chancellor is still hoping that his country will avoid a recession—and help him stay in power

Get article background

WITH Germany's economy having stopped growing in the second quarter of this year, unemployment up for the last seven months in a row and the government's ratings slipping sharply, many Germans have begun to wonder whether their hitherto unstoppable chancellor might at last begin to falter as next year's general election approaches. Gerhard Schröder's mantra that he would use a "steady hand" to steer Germany through the gathering economic storms has begun to sound alarmingly like shorthand for doing nothing. Nearly two-thirds of Germans say they are unhappy with the government's performance.

Some pollsters say that if an election were held today, the conservative opposition, the Christian Democrats, in alliance with Germany's liberals, the Free Democrats, would dish Mr Schröder's coalition of Social Democrats and Greens. Worse for the chancellor, his coalition had shown itself divided over the question of sending German troops to help keep the peace in Macedonia—and even seemed in danger of being defeated in parliament over the matter. Mr Schröder was starting to look as if he was on the ropes.

This week, however, with the Macedonia vote in the bag, Mr Schröder has once again shown fellow Germans his mettle. By contrast, it was the vacillating Christian Democrats who looked divided, indecisive and perilously bereft of firm leadership. With a government majority of only 16 in the Bundestag and a threatened rebellion by 39 of its backbenchers, Mr Schröder's victory had been far from assured. The Christian Democrats had said they would vote against deployment of German troops unless the government agreed to pump at least DM500m ($232m) into defence. In the end, they got a promise of an extra DM28m for the Macedonia mission. But faced with growing dissent within their own ranks, and opinion polls showing that two-thirds of Germans wanted to send troops, the Christian Democrats' leaders had to change tack. They called first for a free vote and then for a vote in favour. In the event, nearly a quarter of the Christian Democrats' 198 deputies voted against.

That left the right-wing opposition in tatters, with the authority of its leader, Angela Merkel, sorely undermined. Once again, doubts are being raised about her suitability to lead the right into battle against Mr Schröder next year. Even before this latest setback, a large majority of voters on the centre-right had said they wanted the more experienced and sophisticated Edmund Stoiber, the powerful boss of the Christian Social Union, the Christian Democrats' Bavarian sister party, to lead the fight against Mr Schröder. The two conservative parties have always insisted that they will not choose a joint candidate for chancellor until early next year. But many are beginning to think it might be better to hurry that decision up.

In any event, the vote on Macedonia was not Mr Schröder's sole victory of the week. He also persuaded Volkswagen (on whose supervisory board he used to sit) and the trade unions to clinch a dramatic new wage deal based mainly on productivity. This showed once again that behind the fixed smile and smooth manner is a tough *Macher*, a fixer, with strong nerves. His promise to provide that steady hand should in no way, he insisted, be equated with the habit of *aussitzen* ("sitting things out" while waiting for storms to blow over), the preferred political tactic of his Christian Democratic predecessor, Helmut Kohl.

Yet many have begun to wonder whether Mr Schröder is not doing just that. Europe's biggest economy has been marking time since the start of this year. Most economists now guess it will grow by barely 1% in 2001, against last year's 3%. Germany, long the powerhouse of Europe, has turned into its biggest laggard. The number of Germans without jobs crept up in July to nearly 3.9m, its highest level in a year, and looks set to go on rising. Even Mr Schröder has now admitted that he may not be able to bring the figure down, as he promised, to 3.5m before the general election expected to be held on September 22nd next year.

"Chancellor, do something!" begs *Bild*, Germany's biggest-selling newspaper. In particular, many pundits urge him to speed up the introduction of tax cuts due in 2003 and 2005. But Mr Schröder says that he will not be rushed into taking panic measures.

His biggest hope is that the economy will begin to perk up before the end of this year. There have been some flickers of optimism. The Ifo business-climate index, which was at its lowest ever in June, rose slightly—against nearly all expectations—in July. New industrial orders, which had been dipping earlier in the year, went up in May and June compared with the two previous months. Despite the global slowdown, Germany's car manufacturers are still notching up record sales. Even the crisis-ridden building industry offers a glimmer of hope, with orders up by nearly 4% in June, the first rise in activity for two years.

Other figures also suggest that Germany's economy may prove more robust than some fear. Revised government figures show an unexpected jump in consumer spending of 1.2% in the 12 months up to the end of June, suggesting that this year's tax cuts may be having a good effect already, though they may also widen the public deficit, perhaps to nearly 2% of GDP. Inflation, which rose in May to 3.5%, its highest annualised rate for seven years, fell back to 2.6% in July, raising the hope of a cut in interest rates in the euro zone.

So gloomy talk that Germany is slipping into a recession may be receding. The economics minister, Werner Müller, a man without a party label who is not usually known for his optimism, is now predicting that Germany may bounce back, growing by 3.5% in the first half of next year—a much faster rate than most economists forecast. Mr Schröder has not yet sailed his way through the storms. But the outlook is less frightening than it was.

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Dutch politics

Wim Kok bows (almost) out

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After almost eight years as prime minister, Wim Kok is ready to depart

HE WON'T leave office quite yet. But with fresh elections due next May, Wim Kok, aged 62 and with almost eight years as the Netherlands' prime minister under his belt, is ready to hand over the leadership of his Labour Party. This week, confirming months of rumour, he told his colleagues so, and named his successor. A new era of Dutch politics—less so of government—is about to begin.

Mr Kok's party does not believe in socialism. Its current coalition partners—Dutch voting habits and rules almost guarantee coalitions—are D66, a vaguely progressive party, and VVD, liberals in the continental sense—meaning originally anti-clerical, and these days on the free-market right. Yet Mr Kok made his way into parliament, and rapidly to a portfolio, by an old-fashioned route: a dozen years as leader of the country's main trade-union confederation.

His chosen successor—there is no other challenger in sight—is a very different figure. Ad Melkert was a professional politician from the start. Now aged 45, he is of variable views, has a sharp brain and as sharp an eye for opportunities, and a keen admiration for Britain's Tony Blair. He has been the party's floor leader in the lower house since 1998.

"A nice man with a good sense of humour," says a colleague there. Yet Mr Melkert is distinctly short on what Mr Kok has in abundance: charisma. Opinion polls put him far down the popularity league. And this week he was under a cloud, cast by a report into misuse of European Union funds in the days, 1994-98, when he was social-affairs minister. In his view, it left him in the clear, and no one suggests the money, aimed at getting people into jobs, went into his own pocket. Maybe not, said the media, but plainly he had not done his job of controlling just where it did go.

Though Mr Kok plans to stay prime minister until a new government is formed (which could be many weeks after election day), he will hand over the party reins late this year, amply soon enough for Mr Melkert to make his public mark. Yet the popular Mr Kok's departure will hurt a party already at some risk. So far, the Dutch economy has felt surprisingly little of its German neighbour's distress. Unemployment is very low, public finances healthy. But this may not true by next May. In 1998, Labour took 45 seats out of 150, to the VVD's 38. Next year the liberals have a chance of edging ahead. That would be most unlikely to cost Labour its place in a coalition; but it would very probably cost Mr Melkert the prime ministership.

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Scandinavia's republicans

On the rise

Aug 30th 2001 | STOCKHOLM
From The Economist print edition

Two out of Scandinavia's three monarchies look a bit less secure

ON THE face of things, Scandinavians enjoy the paradox of being sturdy monarchists and relentless egalitarians all at once. Judging by the whoops and cheers in Oslo's streets last weekend, when Norway's crown prince married a commoner with a four-year-old child born out of wedlock with a convicted drug offender, many still feel that way. But republican sentiment in Norway and Sweden is far from dead. In the past week, two of Scandinavia's biggest newspapers have called for their countries' monarchies to go. Only Denmark's popular royals have been largely unscathed.

Dagbladet, whose Saturday edition is said to be read by a third of all Norwegians, marked the prince's wedding day with an editorial calling for a republic. And Sweden's *Dagens Nyheter*, the country's largest and most influential daily, surprised many of its readers by demanding the same in Sweden. "Royalty and the public should both be freed from the anachronism of a hereditary monarchy", its editorial opined. Sweden's head of state (or monarch, if people still want one) should instead be elected.

Not that the constitutional monarchies of Sweden, Norway or Denmark are under immediate threat. All three have been rather good at reflecting their people's worthy tastes. Indeed, a recent opinion poll said that four out of five Swedes still want a monarchy, while their king, Carl Gustaf, always scores well in the country's annual popularity contest.

But this sudden surge in republican spirit in the media suggests that things can change fast. Norwegians' support for their monarchy has dipped sharply. A decade ago, some 80-90% backed it, but a poll earlier this year put the figure at 58%, the lowest ever recorded. This went up a shade, to 62%, on the eve of the recent royal wedding. But several prominent Norwegians, including Kjell Magne Bondevik, a former prime minister who leads the opposition Christian Democrats, have raised questions about the monarchy's future.

Most mainstream political parties in Norway and Sweden say they are content to let their monarchies be. But ever more intrusive and irreverent press coverage is subjecting Nordic royals to new and unfamiliar pressures. Sweden's tabloids compete to examine the minutiae of Crown Princess Victoria's purported romantic attachments. King Carl Gustaf and Queen Silvia were infuriated two years ago when some Swedish newpapers published pictures of a thin-looking Victoria and suggested that she had an eating disorder. This month pictures evidently taken with a long lens were published of Victoria's younger sister, Madeleine, passionately embracing a friend on holiday.

Royal Danes, however, are still treated more kindly—and their country's monarchy looks less vulnerable to republican assault. Crown Prince Frederik, a dashing 33-year-old, was last year voted "man of the year" for the fourth time in a row.

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Italy's new government

Flying some daring kites

Aug 30th 2001 | MILAN
From The Economist print edition

Will Italy's prime minister act as radically as his people talk?

EVERY other day of the hot summer holidays, it seems, one of Silvio Berlusconi's new ministers has been floating a kite. Out flies an idea in a speech or interview, the opposition on the left dissents, arguments break out in the press and sometimes even within the new government, and then Mr Berlusconi's spin doctors and pollsters measure the general reaction. By the time parliament returns in two weeks' time, priorities and possibilities will become plainer, and legislation can begin in earnest. That, at any rate, is the new team's strategy.

Grand enough for Berlusconi?

The kites have so far trailed some radical ideas concerning labour laws, choice in education, public pensions and building a grand new national infrastructure, especially in Italy's blighted south. On the whole, Mr Berlusconi's own name has not specifically been attached to these kites. Instead, he has let his ministers put them up—and then take the flak.

Giulio Tremonti, his economy minister, has probably been the most provocative. At a meeting of an influential group of business-minded Catholics in the seaside resort of Rimini, he suggested junking the old laws on hiring and firing. The main statute on which they are based, dating from 1970, says that nobody can be sacked except "for a just cause". Hitherto, governments of the centre-right as well as the centre-left have been scared to challenge it. Mr Tremonti is less reticent. He says that companies should be able to hire and fire more freely. Too bad, he implies, if the trade unions squawk. When Sergio Cofferati, leader of the largest union complained, Mr Tremonti promptly dubbed him "the archetype of the new reactionary".

In a country where economic governance has long been underpinned by *concertazione*, whereby employers, the unions and the government decide things together, Mr Tremonti's comments were bound to court controversy. Not surprisingly, he has won plaudits from many of Italy's more dynamic businessmen, who feel frustrated by the country's labour-market rigidities. Antonio Fazio, the central bank's governor, is also behind him. And the new industry minister, Antonio Marzano, insists that if firing were easier (albeit with reasonable notice given before dismissal, plus a decent pay-off), companies would be more willing to take on workers with full-time, open-ended contracts; more and more workers these days are on short-term contracts.

The new education minister, Letizia Moratti, has also stirred debate by saying that parents should be able to choose between private and state schools for their children—and be subsidised if they go private. The snag is that the constitution prevents the state from helping private schools. Then change the constitution, says Ms Moratti. "Even post-communist constitutions like those in Croatia, Estonia, Bulgaria and Hungary give parents choice," she says. But the opposition argues that state schools would suffer.

Another idea concerns pensions. Italian workers in private companies pay a third of their gross salaries towards their pensions, against 22% in Britain, 20% in Germany and 15% in France. Among EU countries, only Austria sees more of its GDP go towards public pensions. Italians still retire younger than other Europeans. An Italian can become a pensioner at 55 after working in the public sector for 35 years. Reforms in the 1990s mean that such pensions are becoming steadily less generous and, in their present form, will be phased out by 2008. But Mr Tremonti is said to want them ended by 2004.

One of the biggest kites has the word infrastructure emblazoned on it, plus a figure of *euro*97 billion ($88

billion), which Mr Berlusconi's people say is the sum needed to boost the south. Half of it, they suggest, should come out of the budget, a third from private investors and a fifth from the EU. High priorities are a bridge to link Sicily with Italy's mainland; a new motorway from there to Salerno, just south of Naples; and another between Florence and Bologna. The government also wants to bring water to the drier regions of the south.

These kites have fluttered across Italy's political skies before. It is possible that Mr Berlusconi may deem the reaction to some of them too hostile to warrant his risking his own popularity by enacting laws along the lines suggested. Still, his team has moved fast to test public opinion. And if the tycoon-turned-politician has the nerve to implement radical reforms in, say, just two of the areas under discussion, he will have achieved a lot.

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Spanish scandal

Who's next?

Aug 30th 2001 | MADRID
From The Economist print edition

Some juicy scandals are jangling the government's nerves

NO SILLY season for Spaniards this year. Instead, genuine scandals have filled the headlines—and shown up systematic faults in Spain's supposedly modernised business culture.

The first involved Sintel, a telecoms outfit sold five years ago by the then state-owned Telefonica to a Miami-based leader of the Cuban exiles, Jorge Mas Canosa, who happened also to be a pal of many people in Spain's ruling centre-right People's Party (PP). Mr Mas Canosa, now dead, stripped Sintel's assets and failed to pay Telefonica. So Telefonica stopped subcontracting work to Sintel, which in turn last December sought to fire most of its 1,800 staff. Many of them began to camp outside the finance ministry; the state got them into the mess, it must help them out, they said. In vain the ministry argued that this was a private affair. Public opinion backed the protesters, and as July ended, Jose Maria Aznar's government surrendered. It made Telefonica—albeit by now supposedly in the private sector—hire many of the employees, while the rest got early retirement and state pensions.

Next came the collapse of Gescartera, a stockbroking house run by an ambitious financier, he too with well-placed friends: a complex tale of greed, nepotism and fraud that cast a vivid light on Spain's traditional old-boy network in business. Antonio Camacho's clients included bishops, showbiz stars, the navy's pension fund and ONCE, a huge lottery-running charity for the blind. He promised them record returns on their investments. In fact, he was registering record losses, while acquiring a wardrobeful of Armani suits (estimates ranged from 100 to 2,000), a garageful of flashy cars and several bodyguards. Mr Camacho is now in jail while his dealings are investigated; some $100m is astray.

Chop, chop!

The scandal claimed one early political victim, Enrique Gimenez-Reyna, a junior minister at the finance ministry whose sister was managing director of Gescartera. He resigned in July, denying any links with Gescartera except putting his own savings there. Later, newspapers claimed that meetings he had arranged with officials helped Mr Camacho get ONCE's business. Two heads have rolled at ONCE, and others may follow, notably at the CNMV, the stockmarket regulator, which failed to act in time despite its suspicions of Mr Camacho. He, meanwhile, had lavished gifts on CNMV employees. An outgoing vice-president (and former PP parliamentarian) got a Cartier watch. Two inspectors got nice jobs with Gescartera. Some Gescartera clients received quiet tip-offs that it might be an idea to withdraw their cash. Most did not.

The government has ordered a full investigation, and punishment where it is due. A parliamentary committee will look at the affair too—though not for very long, if PP members have their way. The church has had to defend its decision to invest in Gescartera: one bishop said it was his Christian duty to get the best returns on the donations of the faithful.

The Socialist opposition has been making the most of the affair. Financial scandals milked by the PP played a big part, in the mid-1990s, in bringing down the long-running government of Felipe Gonzalez and his Socialists, who now see their chance of revenge. "We do not seek to make political capital from the misery of many small investors who have lost all their savings," said their leader, Jose Luis Rodriguez Zapatero, from his seaside retreat, while doing exactly that.

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Turkey's poor

Their lot gets worse

Aug 30th 2001 | ANKARA
From The Economist print edition

But apathy still outweighs anger

SUPPER for Ahmet Cimli, his wife and three children is a watery soup made from discarded bones donated by a friendly local butcher; breakfast is a few tomatoes and some stale bread sold at a nearby factory at half the price of fresh loaves. Since Mr Cimli lost his job wiping cars' windscreens at a petrol pump, his family has had to forgo lunch. Such is a typical diet for poor people in the Yenidogan slum district of Ankara, Turkey's capital.

The Cimlis' lot, like that of most poor people in Turkey, has worsened seriously since the economy dived during last February's crisis. Some 600,000 Turks may have lost their jobs; by the end of June, officially registered unemployment had risen by 42% in a year; many hundreds of businesses have folded; and the Turkish lira has shed half its value, eroding the purchasing power of millions of Turks. Inflation at last count was running at an annualised rate of 65%.

Suicides, domestic violence, prostitution and petty theft are all up. A furious man recently parked a tanker in front of the prime minister's office in Ankara and began shouting "I'm hungry! I can't feed my children!" before being hustled away by police. In stormy debates aired nightly on Turkey's widely viewed private-television channels, the possibility of a "social explosion" is frequently discussed.

So far, the mood is surprisingly quiescent. "Turkish society is very resilient and there's still a strong sense of community," says Ajay Chhibber, the World Bank's Ankara man. This summer, the Bank agreed to fork out $6.2 billion in loans for Turkey. Nearly a tenth of that sum is supposed to help Turkey's poor, with the first dollops being given out this month.

The pain of poverty is softened in various traditional ways. Poor people invoke feudal and clan allegiances to solicit help from the better-off. Islamic brotherhoods provide their own welfare safety-nets. The urban indigent in the shanty towns that have mushroomed around Ankara, Istanbul, Izmir and other big cities often seek out people who hail from the same original village or district. But such rural ties are getting weaker.

As poverty bites, cheating increases too. Oguz Isik, a sociologist at Ankara's Middle East Technical University, explains that many poor Anatolians who have made good in the cities have done so by exploiting the *gediks*, a much-used Turkish word meaning loopholes in the law. Politicians, in turn, promise to turn a blind eye to people who squat or build illegally on state land or who dodge taxes—in exchange for their votes.

"We have a system in which everyone from top to bottom cheats and cuts corners—which is why our politicians have never been held accountable," says Mr Isik. But with little spare land left for squatting on and with the government's coffers virtually empty, Turkey's poorest 5%, whose income last year was reckoned to be $395 a head, may well get even poorer.

The latest crisis has brought a new feature: this time, Turkey's middle class has been badly hurt too. Thousands of people working in banks have been sacked. A recent opinion poll in a mass-circulation newspaper, *Hurriyet*, found that some 70% of respondents had contemplated emigration. The number of Turkish applications for the annual "green-card" lottery to win a residential visa to the United States has jumped fivefold this year.

With growing despondency at home, it is perhaps surprising that unrest has not broken out. Apathy, so far, has outweighed anger. Like many intellectuals on the left, Ece Temelkuran, a young female writer, blames the generals' coup in 1980, their third such intervention since the second world war. "Everyone

with a good brain was locked up, the next generation was ordered not to think, the result is that no Turk is willing to take risks or responsibility to improve his lot," she complains.

Moreover, many of the curbs on trade unions and political parties which the generals wrote into Turkey's constitution in 1982 still apply. That is another reason why Turks find it hard to express grievances collectively. And the police remain ready as ever to use their batons against demonstrators who refuse to disperse.

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Charlemagne

Boris Trajkovski

Aug 30th 2001
From The Economist print edition

Like his country, Macedonia's president has to manoeuvre to stay in place

Get article background

SINCE 1999, Macedonia has played host to a startling variety of guests for a small and struggling country. Not all were welcome; and their reception has depended much on just who was manning the reception desk. Among these, one of the good guys—by western criteria—has been President Boris Trajkovski.

The first and least welcome tour group, if that's the word, arrived in the spring of 1999, a few months after an election victory by the current prime minister, Ljubco Georgievski, and his political party, VMRO, the most moderate of several groups claiming descent from a Slav-nationalist guerrilla movement a century ago. Fleeing Serb atrocities, ethnic-Albanians were pouring out of the neighbouring Serbian province of Kosovo in their hundreds of thousands towards Macedonia. Mr Trajkovski, a deputy foreign minister under Mr Georgievski, was among those who urged that the borders be opened to them.

Reluctantly, under western pressure, it was done. But do not judge that reluctance harshly. The decision was not the easy one that mere human decency might seem to dictate. Macedonia's Slav majority do not love Serbs just because they too are Slavs. But nor did they love the refugees just for being the Serbs' victims. Macedonia also had an uneasy ethnic balance, and its own minority—a large one, 30% or so—happened to be ethnic-Albanian. Imagine, say, some disaster or civil war pushing a few million Mexicans northwards. Would any American president find it merely natural—forget domestic politics—to open the gates?

Macedonia's agreement to do so won it the backing of western countries, and then a new bunch of guests: thousands of NATO troops on their way to Kosovo, who needed Macedonia's airport and road links with Greece for their supply lines. It's true they brought lots of hard currency as well, but not nearly as much as their governments and aid agencies were soon to pour into Kosovo. That imbalance has mightily irked Macedonians.

By the end of 1999 Mr Trajkovski, aged only 43, was president, for much the same reasons that had caught Mr Georgievski's eye in the first place. Educated, in law, at Skopje University and then at a Protestant theological college in the United States, he had brains, skills and, not least, that command of English which endears foreign politicians to Americans. What he lacked was political savvy; fine, he would do the job, without causing trouble. He duly got the party nomination, and won, after a much-disputed but not disgraceful election, aided by the votes of many ethnic-Albanians who were disillusioned with the former governing party led largely by ex-communists, and ready to risk voting for a reformed Slav-Macedonian nationalist instead.

Since then, with western support, he has acquired political weight of his own. And a bit more political awareness. Two years on, Mr Trajkovski and most of his fellow citizens this week watched stony-faced as yet another NATO force assembled in Macedonia. This time the visitors' purpose is to collect weapons from Macedonia's own ethnic-Albanian guerrillas—but as part of a deal that many Slav Macedonians think a damned sight too generous to that minority. And like many others, the president blames Macedonia's troubles on NATO's kid-glove treatment of armed ethnic-Albanians in Kosovo.

Still, the deal had been made, with Mr Trajkovski's backing, however hesitant. Without that, no amount of NATO pressure would have got it even on to paper, let alone off the ground. It may fall apart. But at least in theory the rebels will disarm, parliament will ratify the deal, and the minority, mollified by constitutional changes giving wider rights for their language and more representation in the police, will

settle down with their fellow citizens. If so, be grateful to decent Mr Trajkovski.

Maybe to his upbringing too. He is from the south-east, close enough to both Greece and Bulgaria to teach him the need to live with one's neighbours, and far enough from any ethnic-Albanian region to save him learning to dislike such people. And he has learned about minorities from being, in religion, part of one: as a Methodist preacher, he espouses a version of Christianity even rarer in the Balkans than in its British homeland.

Two divides to straddle

Don't bet yet, though. Mr Georgievski has become increasingly nationalist, and the interior minister, Ljube Boskovski, always was so. Tension was high—on the ground and at official level—as NATO began collecting weapons surrendered by the rebels, with the government claiming they hold far more than the few thousand that would satisfy NATO. The parliamentary debate opening on August 31st promised to be heated. And with elections supposed to be held in January, the government cannot afford to anger Macedonia's ethnic majority by looking too soft on the minority or too subservient to NATO.

The country and its president also have another divide to straddle. He looks westward, and accession to the European Union and NATO is Macedonia's obvious way forward. Yet even as British and French troops poured in, the forces of geography and of self-preservation for a small country surrounded by unloving larger ones took Mr Trajkovski last week east to Kiev to celebrate the tenth birthday of an independent Ukraine, the Macedonian government's best ally and main arms-supplier against the ethnic-Albanian rebels. There also was Russia's Vladimir Putin; he and his Ukrainian counterpart, Leonid Kuchma, warmly backed Macedonia in its fight with the rebels—and blamed NATO's mishandling of Kosovo for many of the Balkans' current problems.

The Russians have not played the active role in Macedonia's troubles that they sought and to some extent succeeded in playing in Kosovo. But they are there, and may not be reconciled to watching the West reign undisputed in what they once saw as their own backyard. That's global politics; it is also the politics that can be made use of by a small country and by its president, both manoeuvring among greater forces they do not control.

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Health

Medicine sans frontières

Aug 30th 2001
From The Economist print edition

Health care is opening up to international competition. Those who have been waiting too long for operations will benefit

Get article background

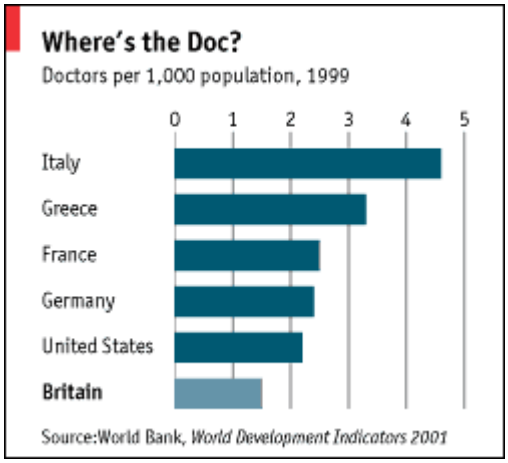
COUNTRIES, like families, tend to criticise themselves, but still feel aggrieved when they are assailed by outsiders. A case in point is England's National Health Service (NHS), which is both cherished (for the ideal of universal free medicine it represents) and increasingly despised (for the quality of care it actually delivers). But those who seek to change it do so at their peril. Plans recently announced by the government to recruit more foreign doctors, and for NHS patients to be treated abroad, have predictably produced angry reactions. Both ideas make sense, though they have important implications for the future of health care.

Is there a doctor in the hemisphere?

Last week the *Daily Mail*, a big-selling tabloid, published a cartoon depicting a black witch doctor, straddling the bed of a terrified white patient. A nurse demands: "Answer the doctor...have you drunk your warm cockerel's blood this morning?" This racist joke was prompted by a government drive to recruit doctors in Australasia, North America, Europe and elsewhere, to help fulfil a pledge made last year to recruit nearly 10,000 new doctors by 2005. Opposition politicians have decried the international recruitment campaign as evidence of the government's failure.

Such carping is economically illiterate. Foreign doctors already account for around half of all those registering to practice in Britain. In total, the number of new registrations last year was the lowest since 1992—because an upturn in the number of British registrations was balanced by a decline in foreign ones. Indeed, one of the reasons for Britain's current shortfall is that many doctors from Asia who came to Britain in the 1960s have reached retirement age. On the other hand, more foreign nurses are likely to register in Britain this year than indigenous ones.

The NHS inherits all this expertise without paying for the training. Indeed, the attractions of foreign staff to the NHS are more obvious than its own appeal to them. Doctors' pay in Britain is higher than in some southern European countries that have a surplus of them, but so is the cost of living. Statistics on the number of patients per doctor reinforce anecdotal evidence about the heavy workload in Britain: there are twice as many physicians per thousand population in Greece, and three times as many in Italy (see chart). The government won't be advertising in developing countries, after an intervention by Nelson Mandela curtailed the active recruitment of South African nurses. Elias Mossialos, of the London School of Economics, says that doctors attracted to the NHS are unlikely to be the experienced specialists it most needs.



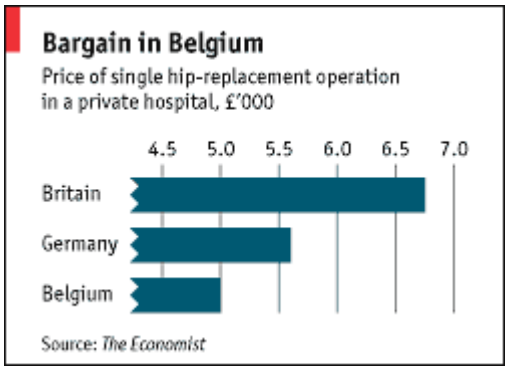
Taking the mountain to Muhammad

In health, as in other industries, the raw materials can sometimes be moved to where there is skilled labour, rather than vice versa. Some frustrated British patients pay to have their treatment abroad. The number of NHS patients waiting for hospital treatment in England is stubbornly stuck at around 1m; at the last count, 46,000 had been waiting for more than a year. Until now, though, the NHS has paid for only a tiny number of exceptional cases to be transferred to foreign hospitals.

But last week the government abandoned its resistance to exporting more patients. The catalyst was a ruling made by the European Court of Justice in July. It confirmed that health care was, in principle, covered by the EU's laws on the free movement of goods and services. It also said that patients were entitled to seek treatment abroad, unless it could be provided domestically without “undue delay”. “Undue delay” is the sort of concept that gets the lawyers excited. Lest they get involved, Alan Milburn, the health secretary, has said that NHS organisations will in future be able to sign block contracts with foreign hospitals.

Cue for more angst among those who think the NHS should be self-sufficient. But when the scheme, and the patients, take off, the little-Englanders will probably be outnumbered. Frank Field, a former Labour minister, thinks this could be as much of a vote-winner as the Tory scheme to let council-house tenants buy their homes. Perhaps, having pledged to “save the NHS”, ministers previously felt it would be humiliating to rely on foreigners. But failing to meet their pledge would be much more hazardous.

The government says that a shortfall of staff, rather than of cash, is now the NHS's main problem. But exporting more patients could save cash as well. Paying a premium for speed can be economical, given the extra medical costs and lost tax revenue incurred through delays. And for some conditions, export will simply be cheaper: spare capacity in continental hospitals—not necessarily something to be proud of, since on a large scale it betokens inefficiency—means they can offer competitive rates (see chart).



Specific comparisons are tricky because travel costs, bulk discounts and varying medical practices need to be considered. But Keith Smith, of Euromedic, which helps to transfer NHS patients to private hospitals, says that Belgian, French and German ones are generally cheaper than British hospitals, and the government is already sending some NHS patients to them. GerMedic, a company that is arranging treatment for Norwegian patients in Germany, says it can offer a hip replacement for £6,500 ($9,425), roughly the same as in Britain—including travel, and a week in Germany for a companion.

Nowhere to hide

Perhaps a helping hand from Europe will boost the EU's popularity in Britain. But, for the government, two problems may arise from the increasing mobility of doctors and patients. Martin McKee, of the London School of Hygiene and Tropical Medicine, thinks that there will be an increasing need for a health policy developed at a European level, to co-ordinate standards and training: in theory, all doctors who qualify in the EU are equal; in practice, some are more equal than others.

But more important than the pressure to centralise will be the power that accrues to patients. As increasing numbers return from the continent with tales of quicker and better treatment, the more difficult it will become to keep the rest satisfied. Of course, many ailments are not portable. So health care can never be just another industry that Britain can give up on. In the future, though, it won't be so protected from international competition.

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Schools

Those who can, won't

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The teaching profession needs a good recession

MIKE TOMLINSON is head of Ofsted, the schools inspection service. Rekindling memories of his headline-grabbing predecessor, Chris Woodhead, Mr Tomlinson picked the week before the start of the new school year to claim that teacher shortages are at their highest level since 1965, and that 40% of teachers are quitting before completing three years in the classroom.

There was a predictable outcry, with bold headlines warning of four-day school weeks and cancelled courses. However, as Mr Tomlinson himself admits, there is little more that the government can do to attract more teachers into the profession.

Mr Tomlinson arrived at his 40% figure by conflating the 15% who drop out from their teacher-training courses with the 25% who leave within three years of starting work. In fact, these figures are not exceptional within the context of the modern labour market. More young people are switching jobs at the beginning of their career than ever before.

There has been a shortage of teachers for the past four years. During the summer, schools now regularly scour the world looking for teachers, mainly from the Commonwealth countries. Over the past ten years, about 25,000 teachers have been recruited from New Zealand, Australia, South Africa and Canada.

The reasons for the domestic recruitment crisis are not hard to find. Contrary to popular perception, teachers are well paid compared with some of their foreign counterparts. The problem is that their pay does not compare favourably with that in other professions in areas of economic boom. Thus in the economic hot-spot of the South-East, London has 1,000 vacancies, whereas in sluggish Wales there are none.

As most acknowledge, the government has done a lot to ease the problem. Low-interest loans have been introduced to help teachers to buy cheaper homes in the South-East. The government has introduced teacher-training salaries, "golden hellos", performance-related pay and other incentives to persuade ex-teachers to come back. In an economic slowdown, these packages will begin to look more attractive.

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Men's magazines

Drooping

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From The Economist print edition

The men's magazine market is in trouble. Does that mean men are too? Or is it simply that the lads' culture is fading?

LOADED, explained its first editor, James Brown, was "for the man who believes he can do *anything*, if only he wasn't hung over". When the original British lads' mag was launched in 1994 by IPC magazines, now part of AOL Time Warner, it disproved the publishing dictum that there was no mainstream market for a general men's magazine. The sort of grooming and fashion fare supplied by the existing glossy titles, such as *Arena*, *GQ* and *Esquire*, went the line back then, was only for a small minority. True, but no one had explored the alternative, which was to fill pages with semi-clad women and stories about sex and football, all written in a jocular, demotic style that could pass for irony.

Loaded's success spawned a gaggle of imitators: *FHM*, *Maxim* and *Men's Health. FHM*'s sales far outstripped those of *Cosmopolitan*, the leading British women's monthly. And "the *Loaded* generation", a term usually employed with contempt, even crept into debates in the House of Commons.

Now, however, the lads' mags are in trouble. In the first six months of this year, sales of 11 of the 15 titles classified as men's magazines, including *Loaded*, dropped from the same period last year. In May, Cabal Communications had to shut down *Mondo*, a new title designed for the "post-*Loaded*" generation.

Part of this decline could simply be due to the economic slow-down. Women's titles, such as *Marie Claire*, *Cosmopolitan* and *Tatler*, have taken a battering this year too. But the fall at the lads' mags has been steeper: *Loaded* has lost nearly 13% of its circulation. Even *FHM*, owned by Emap, a British publisher, which remains the market leader with a circulation of over 700,000, was down by 2%.

The disaffection with the men's titles could also be due to the fashion cycle. The irreverent British lads' mags burst into a complacent, upmarket, London-oriented magazine trade and offered something different. *Loaded*, claimed one of its founders, Tim Southwell, was a "magazine which unashamedly celebrated working-class Britain: football, drinking, sex". This unapologetic celebration of in-your-face heterosexuality was a studied antidote to the prevailing political correctness. "The new lad," says Ben Crewe, a sociologist at Essex University who has researched the subject, replaced the "new man" as the "dominant metaphorical motif for the conceptualisation and representation of contemporary masculinity."

But, as the lads' mags draped increasingly undressed bodies of increasingly unknown women across the covers, so the upmarket titles followed. Today, all the men's magazines look pretty much the same. This month, the cover of *GQ*, once graced by John Major, is filled mostly with the ample bosom of Jordan, a model, with the caption: "Naked ambition: How did Jordan get so, well, huge?"

Indeed, the market has become so bland that there are now the stirrings of differentiation. Most notably, Peter Howarth, editor of *Esquire*, last year decided to put an end to semi-naked women on the cover and go for something classier. Sales plummeted by 30% in the six months following the change. But, says Mr Howarth, the readers who are left are the more upmarket types, so advertising rates are up.

Perhaps the falling sales of the men's titles say something broader about male culture. The lads' mags perfected a celebration of male fecklessness, with an irony that was probably appreciated more by its writers than readers. "For men who should know better" goes *Loaded*'s tagline. Could it be that it is no longer cool for men to be hopeless? David Hart, general secretary of the National Association of Headteachers, thinks so. When last week's GCSE results were published, showing that the margin by which girls outperformed boys had narrowed slightly, he declared: "We may be witnessing the first signs that the laddish culture, which has pervaded for far too long, is on the wane."

So will serious reflection, with its attendant uncertainty and anxiety, replace all that defiant hedonism? As economic times harden, goes this view, so male angst returns. Or perhaps laddishness was really about male anxiety all along. “The lads’ mags are all about the denial of the real problems men are facing,” argues Mr Howarth. “The lads’ mags are fantastically in denial about anything serious and are absolutely rooted in nostalgia. This hankering after the past is a way of not facing up to hard times.”

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Exams

D-graded

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From The Economist print edition

Are competing exam boards driving down standards?

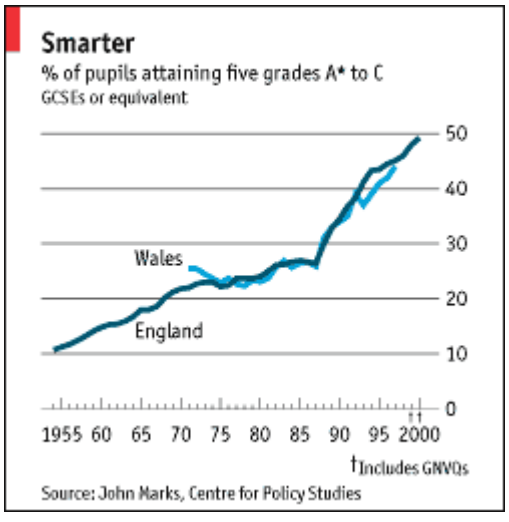
AS USUAL, the government is saying that children have done better in this year's exams than ever before. And as usual, almost nobody believes them. This year, the proportion of GCSE results graded A*-C rose by 0.5% to 57.1%. The improved marks prompted worries about whether standards are improving or exams are getting easier.

Grade inflation is rightly a cause for concern. GCSE exams, normally taken at 16, are the one qualification most school leavers have, and employers should be able to use them to compare their prospective employees. If the value of each grade is diluted over the years, then the results become a devalued currency. The latest theory to explain grade inflation is that exam boards, under pressure from schools wanting to do well in published performance tables, compete by making good results easier to come by.

Trying to work out what causes the inflation is a murky business, because different things can make grades go up. Students may get smarter, and exams may get easier. A third possibility is that the boundaries between different grades shift. When the grade boundaries go down, more students get good marks without any improvement in their work. Last week, a retiring examiner, Jeffrey Robinson, claimed that standards had been progressively lowered over the years to improve students' grades.

So how do the examiners know where to set the boundaries? "At the end of the day, you can only make that judgment when the students have sat the paper," says Paul Sokoloff, who speaks for all the exam boards in England, Wales and Northern Ireland. It would appear that examiners assess how hard a paper is by seeing how well students do in it. Mr Sokoloff admits that there is something rather circular about it. He calls the process "a complex web of check and counter-check".

Unfortunately, this complex web appears to have broken down somewhere. Even if the exam boards are right that students are likely to get better every single year, that does not explain the dramatic rise in pass marks following the introduction of GCSEs in 1988. Nor does it explain why that rise has now slowed down (see chart).



Mr Robinson's suggestion is that as schools find some exam boards harder than others, they opt for the papers that deliver the highest grades. The boards are therefore obliged to compete with each other by lowering standards. Alan Smithers, a professor of education at Liverpool University, says schools have plenty of incentives to choose the easiest boards. "Results have become so much more important recently," he says. He thinks that the growing importance of league tables, as well as new government targets, may mean schools will stay with a board only if they keep getting good marks.

That might explain why the rate of improvement has slowed. Over the past 15 years the number of exam boards has steadily decreased, from more than 20 to only five outside Scotland now. That has made it easier for the Qualifications and Curriculum Authority, a quango that tries to keep standards constant, to compare different papers. But the fact remains that the same qualifications can be reached by different means: some boards will offer more course-work, some exams will have more modules, and so on. So students will presumably find some boards' exams easier than others.

If exam boards are competing with each other to produce easier exams, surely it would be better to have just one exam board? Mr Sokoloff is wary of such a plan. “The move in all sectors of our society has been away from monopolies and towards things that offer choice,” he notes.

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Salmon fishing

Back a-leaping

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Joy for fly-casters

THE salmon is one of nature's great mysteries. How does it manage to swim down its river of birth to roam across thousands of miles of ocean and then find its way back to the same river to begin the reproductive cycle all over again? Never mind. Recently, anglers and river owners have been increasingly worried that fewer and fewer salmon have been travelling upriver. But this year, there is good news; salmon are back in bigger numbers than have been seen for some time.

Nobody is assuming that a 50-year decline in salmon stocks has at last been reversed. But Jeremy Read, director of the Atlantic Salmon Trust, a salmon conservation body, says he has been heartened by reports of big salmon runs coming from the Tyne at Newcastle to the Dee in north-east Scotland.

If there has been better fishing this year, the credit probably belongs to an Icelander, Orri Vigfusson. Ten years ago, he decided that the big problem was that salmon were being caught by trawlermen out at sea. On the basis that catching fish in rivers contributes a lot more to rural economies than does trawling, he persuaded various river owners and recently governments to put money into a fund to buy out the trawlermen.

"We try to help them find alternative fisheries and work for their business," he says. He calculates that he has spent $10m in the past decade and has cut catching of salmon at sea by about 50%. He is not surprised by the news of good salmon numbers in Norway and Canada and in northern Spain, where rivers in Asturias have reported catches up by 68% on last year. "We always said it would take 8-12 years before results would show," he says.

Mr Vigfusson is not finished yet. He is negotiating with Irish coastal net fishermen to buy them out. The Northern Ireland assembly has agreed to put £1.5m into a fund to buy out Ulster's salmon netsmen. Drift netters operating off north-east England are also in his sights; a pre-April ban on such fishing, ordered by the government, is thought to be one reason why spring runs of salmon were better in east coast rivers.

Other issues are still troubling anglers. In Scotland, their current bugbear is fish farming. Salmon kept in cages in sea lochs attract sea lice, which, if they attach themselves to a fish in sufficient numbers, will kill it. The caged fish can be kept clear of lice by regular doses of chemicals. But that does not help wild fish swimming past.

The anglers claim that the spread of fish farming along Scotland's west coast is the reason why the area's rivers yielded 64% less fish in 2000 than in the previous year. The decline along east coast rivers, where there are no farms, was only 9%. The farmers grudgingly accept that they might be part of the problem, but are reluctant to do anything. They claim that the biggest factor affecting salmon stocks is changes in ocean temperature which affect feeding grounds. But quite how this works is as big a mystery as how to hook them.

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Church of England

Counting the doomsday option

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Another public service is in crisis

THE Church of England is suffering from poverty. It has been in a financial fix before, most famously in the late 1980s when the church commissioners lost money in high-risk commercial property deals. The commissioners, who manage the church's large portfolio of stock exchange and property assets, do better now. In 2000, those assets were valued at £4.4 billion, bringing in an annual income of £160m.

The current problem is that the church has underestimated how much it will have to pay out in pensions. So the £160m income from the church commissioners that would normally go to the parishes to support the everyday work of the church now largely has to be used to make good the shortfall. The amount that the commissioners hand over to the parishes has dropped from £66m in 1991 to £22.4m last year. By contrast, pension payments have risen from £58m to £92m.

Retired clergy are living longer. At the moment, their life expectancy is three years longer than the average. The fact that the clergy often live on into their late 80s is, no doubt, a testimony to the benefits of religious life, but must be unwelcome to its actuaries.

As a result, the dioceses, which rely for their income largely on gifts from church-goers, are being asked to provide an extra £11m a year to keep the church running. Already it is estimated that three-quarters of the dioceses are in the red. The dioceses are urgently exploring ways of preventing the church going broke. As with any other business, there are three options; cost-cutting, leveraging the assets or downsizing (presumably outsourcing to other faiths is not an option). There has already been a bit of the first, but it is the last two that cause problems.

Costs have been reduced, to a level where there is some doubt that any more reductions could be made. The bishops have been getting rid of their chauffeurs and even their gardeners. The average clerical stipend of £17,000 has not been increased for years. The MSF union, which represents about 10% of Anglican clergy, recently put in a claim for a 50% increase, arguing that some members had now been reduced to claiming income support.

So dioceses have been looking at other ways to raise cash. Especially in rural areas, many of the more enterprising clergy have been trying to make their fixed assets, the actual churches, work harder for them. With the closure of so many rural post offices, village shops and banks, some see the churches as ideal centres to supply many of these services. A report last year recommended putting hole-in-the-wall cash machines in churches. Certainly, some parishes have explored the idea of having shops attached to the churches, or opening post office counters in the vestry.

The fabric of the church can also be put to new uses. Hundreds of parishes have already negotiated deals with mobile-phone companies to conceal masts and dishes in church towers and spires. As the companies find themselves unwelcome almost everywhere else, such deals can bring in about £5,000 a year.

And then there is always downsizing. As the Church of England is, constitutionally, the "national church", this is the doomsday option. But now, for the first time, several clergy are actively talking about it. They argue that in many areas with local majorities of Muslims, Hindus, Catholics, dissenters or atheists, it is a waste of slender resources to try to keep open churches that attract tiny congregations. It would surely be better to concentrate on the core business, they say. Thus the spectre of disestablishment returns, not as a constitutional issue but as part of a cost-benefit analysis.

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Concorde

Fly the icon

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Any day now the supersonic jet will be cleared for take-off

WHEN an Air France Concorde crashed in July last year, killing 113 people, and the remaining 12 supersonic aircraft were grounded, it seemed as though the ageing plane would never fly again. But, after modifications, including a kevlar lining for the fuel tanks, tougher tyres and a stronger undercarriage, the authorities in France and Britain are close to restoring the airworthiness certificates needed before British Airways (BA) and Air France can restart their transatlantic flights.

BA has spent £17m on the technical improvements, and a further £13m on a revamped cabin and other improvements. Both airlines have upgraded and test-flown one Concorde, and are working on the rest of their fleet. BA needs three operational aircraft to run a daily service and five for a same-day return. The likelihood is that both airlines will re-launch at the same time in October.

In the months after the crash it appeared that BA was keener than its French competitor to relaunch Concorde. But the truth is that Air France did not want to appear insensitive, pushing for a return of the aircraft, after the horrendous accident which happened when one of its aircraft caught fire on take-off from Charles de Gaulle Airport. BA was never in any doubt that it wanted Concorde back in the air. It can make up to £20m operating profit a year carrying passengers between London and New York, at a return fare of around £7,000. The airlines are not prepared to say what fares they will charge, but the 3,500 regular Concorde users (many of whom fly back first class on subsonic flights after a day's work in America or Europe) are unlikely to be price-sensitive.

There may, however, be fewer of them. It is not just Concorde that crashed: the Nasdaq high-tech stock index has plunged and the number of mergers and company flotations has shrivelled. So there will be no bands of investment bankers racing to close deals by zapping between London and New York at twice the speed of sound. BA is spending £1m to lure customers back. BA's boss has already held two parties for regular Concorde customers to show off the improvements, and they will soon be invited on short test flights to get them in the mood. The aircraft's importance to BA, however, goes beyond the money it brings in: the airline reckons its elegant, futuristic icon (even after 30 years) is a key part of its upmarket image.

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Bagehot

The best show in town

Aug 30th 2001
From The Economist print edition

The Tories should worry about their candidates, not just their candidates' ideas

VACATIONING in Umbria, soothed by deferential cypresses, uplifted by the glories of the Renaissance, Bagehot promised himself that he would not write about the downlifting Tory leadership contest in the first week back. But the temptation has proved too strong. The struggle between Kenneth Clarke and Iain Duncan Smith has turned so vicious over the summer that the jaw of even the seasoned political observer drops at the spectacle. Friends who have little interest in British politics, and none at all in the Conservatives, confide that they are looking on rapt, with the same horrified fascination with which a vegetarian observes a bullfight. Labour itself appears transfixed. Tony Blair and his ministers have good reasons to stay out of the headlines while their political opponents tear their own reputations to shreds. But the government's silence is not just tactical. For the moment, the war of Conservative succession is, simply, the best show in town—and still has two weeks left to run.

What makes it so compelling? For a start, it is protracted, bare-knuckled and deliciously hypocritical. In their single televised debate, the candidates talked through clenched teeth of their "respect" for one another, but when it later transpired that Mr Duncan Smith's campaign had attracted some racist supporters, Mr Clarke did not hesitate to imply that there was a whiff of racism in Mr Duncan Smith's own positions. Second, recrimination is more captivating than mere advocacy. This contest is not only about who will lead the Conservatives in the future; it has flushed out into the open umpteen unrequited grievances about the past. John Major has been blurting out the bitterness he feels towards Margaret Thatcher, who passed him the torch in 1990 but then gave succour to the Europhobic rebels, including Mr Duncan Smith, who made his life a misery. Third, the contest is not just about policy but about political personality. In the 1970s, Malcolm Muggeridge, a wry observer of British manners, said that in order to succeed pre-eminently in British public life it was necessary to conform either to the popular image of a bookie or of a bishop. He had Churchill and Halifax in mind, but the bibulous, bonhomous Mr Clarke and the preachy, solemn "IDS" fit the Muggeridge template no less well.

Last, the contest is not only good drama, in the style of the Grand Guignol. Much portentous analysis would have you believe that Conservatism itself has reached a fork in the ideological road: back to the centre and into the euro with Mr Clarke, or deeper into right-wing insularity with Mr Duncan Smith. In one grim variant of this story, the Tories are skewered whichever path they choose. By putting a Europhile such as Mr Clarke at the head of a Eurosceptic party, they condemn themselves to endless division or outright schism. By choosing a supposed "extremist" such as Mr Duncan Smith, they condemn themselves to electoral oblivion. Some commentators argue that a victory for the former soldier would quickly demote the Tories to third party and enable Charles Kennedy of the Liberal Democrats to become prime minister when voters tire of Labour.

Perhaps. Occasionally, as in the strange death of the Liberals in the first decade of the last century, big realignments do occur in British politics. And after William Hague's collapse in June's general election, it would be wrong to make light of the difficulties any successor will face. All the same, reports of Conservatism's demise are in danger of being exaggerated.

Take that presumed fork in the road. Parties do sometimes make fateful ideological choices. But they do not always do this consciously. And sometimes, when they think they are doing it, they are wrong. For example, it became obvious with hindsight that by choosing Mrs Thatcher over Edward Heath in 1975 the Conservatives had made a fateful change in their ideas and direction. Back then, however, Mrs Thatcher was so careful to keep her half-formed philosophy under wraps that the result of their decision was not evident to the MPs who elected her. By contrast, many Tory MPs thought during the trauma of 1990 that in choosing Mr Major instead of Michael Heseltine they would keep the Thatcherite flame alive. They only discovered later that they had elected a middle-of-the-roader whose one big idea was to make compromises in the name of party unity.

Many Conservatives think that the party is at an ideological turning point now because that is what Messrs Clarke and Duncan Smith tell them. But this is a contest in which a special discount must be applied to what the candidates say. Because it is the first in which the Conservatives will let all 300,000-plus party members vote, both must talk up their differences and argue that electing the other would be an act of terminal madness. The truth is rather more prosaic.

Afterwards could be much like before

Whomever they choose, the Tories will remain divided on Europe—just like voters at large, who showed last June that, pending a referendum, they do not see this as the swing issue in British politics. Nor, despite the conniptions about race, will the party have shifted decisively left or right. Though neither bookie nor bishop signed up for Michael Portillo's crusade to drag the party's social attitudes into the 1960s, both claim to uphold the liberal decencies. Both emit familiar Blairite noises about improving the public services, and neither is likely to depart very far from Mr Hague's thinking on taxes and spending.

In one way, this is as it should be. For although he made some policy mistakes, Mr Hague's problem was less a failure of political ideas or positioning than a personal failure to impress himself on voters as a credible and attractive alternative prime minister. That is still the trouble for the Tories. After this summer of fratricidal over-exposure, there is no reason to be confident that either Mr Clarke, a talented man who has come over as arrogant, or Mr Duncan Smith, a new face who has come over as stiff and inexperienced, will fare very much better.

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Japanese electronics companies

Lay-offs with no sign of revival

Aug 30th 2001 | TOKYO
From The Economist print edition

Headline-hitting job cuts will not be enough to turn round Japan's ailing electronics giants

AP

TOSHIBA says that 19,000 jobs will go. Fujitsu is jettisoning 16,000 workers. NEC is adding 4,000 jobs to the 15,000 it already plans to shed. Kyocera is cutting 10,000 and Oki Electric 2,200. And Hitachi, which has yet to break the bad news, may top them all with cuts expected to total 20,000. Were there any doubts about their health, there can surely be none now: Japan's lumbering electronics conglomerates are in pain.

Fujitsu thought it would make profits of ¥50 billion ($420m) this year. Now it says it will make a ¥220 billion loss, the worst in its history. Toshiba is bracing itself for a loss of ¥115 billion. Pleading turmoil in the chip industry, Mitsubishi Electric, another big firm that has been upended by the global technology recession, has abandoned forecasting this year's profits altogether.

Now, of course, is the time to persuade shareholders that a fix is in the works. And along with the job cuts, investors have been offered plenty of other tinkering to cheer them up. Fujitsu, for example, is shrinking its computer hard-disk-drive business, transferring a chip plant to a joint venture with Advanced Micro Devices, an American firm, and considering spinning off several other businesses, such as printers and flat-panel displays. NEC plans to close some chip-making plants in Japan and Britain. Toshiba may merge its memory-chip business with Infineon, a German company, or sell it to Samsung Electronics, a South Korean firm.

Yet shareholders remain unmoved. Toshiba's restructuring plans, unfurled on August 27th, got a half-hearted cheer from the stockmarket. But Fujitsu's shares have hardly budged since it unwrapped its plans on August 20th. NEC's shares, meanwhile, have actually fallen since its latest effort, on July 31st, to convince investors that it could heal itself.

Although Japan's electronics conglomerates make everything from washing machines to bullet trains and toasters, it is their chip businesses that drive profitability. Recently, however, profits have turned into heavy losses as they have been squeezed from two sides. American firms, such as Intel, have better technology. And other Asian producers, notably in South Korea and Taiwan, can make commodity chips more cheaply.

Some Japanese chip makers, including Fujitsu and Mitsubishi Electric, have been abandoning commodity production wherever possible. Toshiba, Hitachi and NEC have, however, dithered badly, neither making the investments to produce on the right scale to compete on price with the South Koreans and Taiwanese nor getting out of the business altogether.

The latest recession, in which the prices of some types of commodity chip have fallen by nearly 90%, has at last prodded some of the Japanese laggards into action. NEC is closing a British plant which makes DRAM commodity chips, and the company is also rumoured to want to sell its stake in a DRAM joint venture to its partner, Hitachi. Selling Toshiba's memory-chip business, says Ikuo Matsuhashi of Goldman Sachs, would add ¥100 billion a year to the company's profits.

The future is confused

The Japanese have a better notion of what chips they do not want to make than of where to turn for future profits. Fujitsu and Mitsubishi have invested in “flash” memory-chip production. Because flash memory is used in mobile phones, cameras and other gadgets, it would protect them, they argued, from a downturn in the PC business. So much for the theory. Thanks to a slump in the mobile-phone business, flash memory prices are also falling fast; one of Fujitsu’s flash memory plants is running at 20-30% of capacity.

Neither Toshiba nor NEC is giving away much about its future sources of growth. “The Japanese are offloading before they have their replacement products in place,” says Roger Mathus, the Tokyo representative of America’s Semiconductor Industry Association. The same point applies to the job cuts. Deep, immediate cuts might persuade investors that the Japanese can soon return to growth. But this is not what they are promising. NEC has given itself three years to hit its targets, as has Toshiba. Hitachi is rumoured to be planning something similarly distant. At this rate, restructuring looks more like managed decline.

Only Fujitsu is promising to hit its job-cut target by the end of the year. But this tells another story. Unlike Toshiba, which is sensibly making its deepest cuts in high-cost Japan, Fujitsu will make 11,400 of its 16,400 cuts overseas, dumping the foreigners, in time-honoured Japanese fashion, to protect more expensive jobs at home. Either way, none of the big electronics companies plans compulsory redundancies in Japan. Despite the savage operating environment, firing long-serving workers is still taboo, a principle around which all restructuring plans apparently have to fit.

Despite the savage operating environment, firing long-serving workers is still taboo

The larger strategic questions, meanwhile, go almost entirely unanswered. As conglomerates, the Japanese are corporate relics, lacking the scale or focus to compete effectively in any of the many industries that they straddle. To create an American Hitachi, for instance, you would need to merge a bit each of Intel, Lucent Technologies, Microsoft, IBM, General Electric and many others besides. All told, the group contains a staggering 1,069 companies.

Outlining his firm’s restructuring efforts, Naoyuki Akikusa, Fujitsu’s president, rejected the notion that Fujitsu should break up its 517 companies, saying instead that he would pursue a “Japanese new-business model”. This week, Tadashi Okamura, Toshiba’s president, waffled hopefully about “synergy effects” among his 323 group companies. But even Mr Okamura’s management consultants have had a hard time figuring out exactly what Toshiba is in business to do. The latest thinking divides the company into three incomprehensibly vague units that between them cover just about all possibilities: industry and society, the individual, and components.

Between them, Toshiba, Hitachi, Mitsubishi Electric, Fujitsu and NEC employ almost 1m people. Hundreds of thousands more supply or distribute to and from them. As in the former Soviet Union, whole cities depend on them for their livelihood. In a week in which Japan’s unemployment rate hit 5% for the first time since the second world war, the massive cuts in their payrolls are provoking panic. What really should worry investors, however, is not how much they are doing, but how much they are not doing.

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Auction houses

Affairs of the art

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We look at the changing ownership of the big auction houses

Get article background

Reuters

Sharon Stone takes to the hammer

EVER since Alfred Taubman, an American property mogul, appointed CSFB, an investment bank, to decide what to do with his controlling stake in Sotheby's, the art world has been rife with rumours of potential buyers. The name most frequently mentioned is Bernard Arnault, the boss of LVMH, a stable of luxury brands which already owns Phillips, a smaller British auction house. If Mr Arnault were to buy Mr Taubman's stake, the world's two biggest auction houses, Sotheby's and Christie's, controlling between them more than 90% of the art-auction market, would be in the hands of Frenchmen.

Christie's was bought in 1998 by François Pinault, the boss of Pinault-Printemps-Redoute, a French conglomerate, and Mr Arnault's arch-rival. Soon afterwards, Mr Arnault looked at Sotheby's but decided it was too expensive. Instead, he bought Phillips in November 1999, with the aim of thrusting it into the premier league.

Since then, he has been spending lavishly on advertising, unusual sales methods and high-profile hires. Sharon Stone turned up at a Phillips auction in New York in return for a generous donation to a charity she supported. Simon de Pury, a respected former chairman of Sotheby's Europe, was brought in with Daniella Luxembourg, a former deputy chairman of Sotheby's Switzerland. Both were armed with impeccable address books; in their honour, the firm was renamed Phillips, de Pury & Luxembourg.

Mr Arnault is also exploiting to the full all the tricks that auctioneers like to use to manipulate the outcome of art auctions. Most auction houses give guarantees (a fixed amount granted to the seller), set a minimum price or reserve below which an item cannot be sold, sell unsold items over the counter, and take bids "from the chandelier"—ie, from a fictional bidder. But Phillips is pushing these practices to new depths in its fierce efforts to dethrone the duopoly at the top. "High guarantees are an easy way to win business if you do not want to make a profit," says Edward Dolman, chief executive of Christie's. "It is distorting prices," complains Robin Woodhead, chief executive of Sotheby's, for Europe and Asia.

Guarantees, which are perfectly legal, rarely pay for auction houses; and they also run counter to the whole idea of an impartial auctioneer. But they certainly help to attract sellers. If an item sells for less than the guarantee, the auction house pays the difference; if it goes for more, the proceeds are usually split between auction house and seller. By giving a guarantee, the auction house has "an interest", as it says in small print in catalogues. It is, in effect, auctioning its own property.

Phillips's strategy of generously underwriting first-rate sales has won it this year's most coveted consignments. In May, Mr de Pury auctioned pictures in New York that belonged to Heinz Berggruen, a much-respected art dealer in Berlin whose son works for Phillips. Alongside the Berggruen collection went a consignment by Henry Kravis, a financier and, ironically, a board member of Sotheby's. Phillips also bagged a prize collection of about 80 works of art belonging to the heirs of Nathan and Marion Smooke, a wealthy couple in Los Angeles. These will go under the hammer in New York on November 5th.

Phillips's tactics for breaking through to the top have been both risky and expensive. The Berggruen pictures sold for $71.2m and probably failed to cover the guarantee, said to be more than $80m. A large Van Gogh landscape and a pretty portrait of a woman by Renoir were left unsold. The guarantee for the

Smooke pictures is said to be $200m, even though the lower estimate for the collection is $140m. This is another risky bet, particularly given the global economic slowdown, which is already affecting the market.

“We are building market share,” says Mr de Pury. But is there enough business at the top for three? Mr Dolman thinks there are only about 50 private collectors who buy works of art for $20m or more. Christie’s, like its competitors, considers the middle market its safety net, in particular when the economy goes sour. It has been doing well thanks to Christie’s South Kensington, its London saleroom for the middle market. Sotheby’s is launching a new saleroom in west London, at Olympia on September 3rd, to reclaim some middle-market share from Christie’s.

Mr Arnault recently bought Bonhams & Brooks, a British auction house that traditionally caters to the middle market. Unexpectedly, he did not merge it with Phillips, but formed two separate entities. Phillips, de Pury & Luxembourg is to focus on the best art, jewellery and furniture, while Bonhams looks after the rest.

This could clear the way for a merger of Phillips and Sotheby’s. Mr Taubman’s stake in Sotheby’s is worth far less than it was two years ago when Mr Arnault last looked at it. Sotheby’s was ordered by a court in New York in February to hand back $286m to sellers for its part in a commission-fixing scandal with Christie’s. This, and misadventures with its Internet strategy, contributed to a loss of $8.3m in the first half of this year. Now there are rumours that it is to announce cuts of up to 20% of its workforce (around 400 people) after America’s Labour Day weekend, as a prelude to selling the business.

Mr Arnault may eventually find it less expensive and risky to buy Sotheby’s than to go for market share by other means. The age-old Sotheby’s-Christie’s battle will then be an all-French affair.

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About sponsorship

French auctioneers

Prised open

Aug 30th 2001
From The Economist print edition

The big French-owned auction houses are at last able to do business in France

Get article background

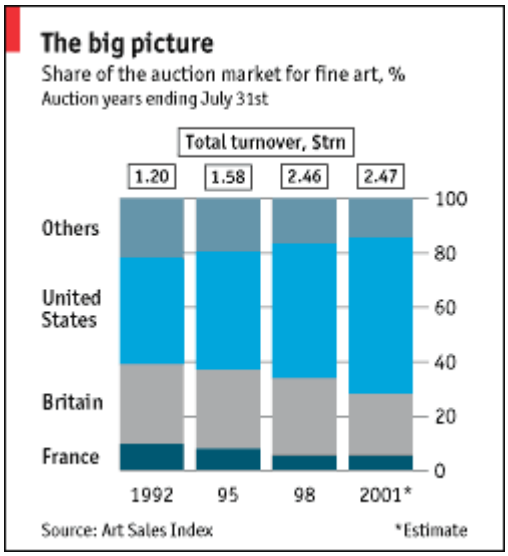
AFTER resisting injunctions from Brussels for almost a decade, the dusty world of French art auctions is at last facing transformation. The much-awaited decree shattering the centuries-old monopoly of state agents—or *commissaires priseurs*—over public art auctions was at long last published in July, more than a year after the law liberalising the market had been approved. Now, once the recently created *conseil des ventes* has approved them, international auction houses such as Christie's and Sotheby's expect to be banging the hammer in France from the start of next year.

The local auctioneers fought to the end. In late June, Sotheby's organised a sale in its posh Paris office, administered by Poulain & le Fur, a dissident firm of *commissaires priseurs*. But it was promptly sued by the city's association of auctioneers, which had to approve any sale not held on its own Drouot location. At the last minute, the event was moved to Poulain & le Fur's office at the somewhat less glamorous Palais des Congrès.

With international art-auction giants authorised to sell in France, competition is likely to spell rationalisation for the 458 *commissaires priseurs*. Some of them—such as Poulain & le Fur, Tajan and Piasa—have already built links with the big houses. But for the reluctant *commissaires priseurs*, there is some good news. They will now be free to set their own fees, which were fixed by law at a level low by international standards.

The reform could also breathe new life into the suffocating French market. Once the world leader—with 90% of the international art-auction market as recently as the 1950s—France now accounts for a meagre 6% (see chart). Foreign auction houses, unable to operate in Paris, have been finding art in France but selling it in New York, London and Geneva.

The effect of the changes, says François Curiel, Christie's European chairman, will be that Paris will grow, but not at the expense of other big markets. The main victims could be art dealers and wholesalers, rather than auctioneers in London or New York. The only auction spot expected to suffer is Monaco, which has been a proxy for Paris for both Christie's and Sotheby's.



For the time being, however, Paris will remain at a fiscal disadvantage compared with London and New York. Britain has until 2010 to comply with a recent European directive on a resale tax payable on contemporary paintings—the proceeds of which are transferred to artists or their families—while America has no such tax. In addition, VAT on art imports is higher in France than in America or Britain. That is likely to make foreign sellers think twice about auctioning their wares there.

But it takes more than tax to make or break an art market. Cities increasingly specialise, and the availability of treasures for sale matters. New York's domination of contemporary art is closely related to the fact that the most prominent contemporary artists happen to be American. Paris is strong in furniture, art deco and rare books. That dominance is likely to be reinforced, not weakened, by the recent change in the rules.

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Time-sharing

They share horses, don't they?

Aug 30th 2001 | BALTIMORE
From The Economist print edition

The tacky business of time-sharing is moving from houses to horses

AS A way of marketing property, time-sharing is a familiar idea. Now stable owners across America are adapting the concept to their business. Riders pay a monthly fee, choosing from plans that offer a given number of days a week of riding, or "unlimited riding time". Typically, for less than $400 a month, riders can saddle up as much as they like without the considerable investment involved in actually owning a horse.

Mike Smith, director of the Columbia Horse Centre near Washington, DC, launched a time-share plan about a month ago which he calls the "Equi-Lease" programme. "It has been a tremendous success," he says. "Rather than a traditional horse lease, where you lease one horse exclusively, you're leasing into a whole stable when you time-share. The fee you pay allows you to ride any one of the horses that are in the Equi-Lease programme any time you want. We do the rest."

Monthly fees amounting to roughly half the expense of stabling, feeding and caring for a horse are attracting the same folk who are sought after for time-share properties. "Baby boomers", many of whom rode nags in their youth, are taking advantage of time-share schemes as an affordable way to reacquaint themselves with the pleasures of being in the saddle. Some of the developers are old time-share hands too. Al Grimsley, owner of the Mountain Trail Rider Ranch near Salt Lake City, Utah, retired from the business of selling time-share property. "So this idea comes naturally to me," he says.

According to a recent study by the American Horse Council, an industry lobbying organisation, 7.1m Americans are involved in the equine industry, which is worth $112 billion a year—making it arguably bigger than the railway, furniture and even tobacco industries. Horse business is big business.

Could time-sharing bring a new wave of middle-aged "Lone Rangers" to the industry? Those adopting this innovative marketing scheme believe it could. "I'm convinced this is the best way to have access to a horse in the future," says Kathy Rutan Sprague, owner of the Daystar Ranch in Red Bluff, California. "I think we'll see a lot more of it. It decreases our overhead and it's best for the horse, best for the rider and best for the stables."

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Mobile phones in China

A billion voices calling?

Aug 30th 2001 | HONG KONG
From The Economist print edition

High hopes for China's mobile-phone market have been dashed

WHICH is the biggest mobile-phone market in the world? The answer, since July, is China's. A country in which, until a few years ago, the only people who could afford mobile phones were triad mobsters now has 121m users. BDA, a Beijing consultancy, forecasts that the number will rise to 370m by 2005, enough to persuade many investors—even after telecoms shares have dived all round the world—that China was, and would remain, a magic market.

AP

Too few farm folk fancy a phone

Over the past few weeks, however, much of that magic has vanished. China Mobile, the mainland's dominant operator, with 73% of the market, announced half-year results that were superb in every respect bar one: average revenues per user were down by 35%. The drop took analysts by surprise and sent China Mobile's shares into a tailspin. Shares in China Unicom, the smaller rival in the country's duopoly, followed. Suddenly, soaring forecasts of market size seemed worth rather less.

Looked at one way, China's market for mobile telephony appears as promising as ever. Fewer than one in ten of the 1.25 billion Chinese has a mobile phone, compared with four out of ten Americans and five out of ten Europeans. In China, reckons Wang Xiaochu, China Mobile's chairman, a penetration of three in ten is achievable within a few years. This is more optimistic than the government's official forecast but still plausible.

But where are the extra two to be found? Most Chinese with any spending power to speak of already have mobiles and use them shamelessly, as anyone who has sat in a cinema in China can attest. To sign up new subscribers, China Mobile and China Unicom are having to reach out to poorer people. One way they are doing this is by offering not the usual service, where users talk and pay the balance of their accounts in arrears, but a prepaid, discounted package. Of China Mobile's 14m new customers in the first half of this year, 95% took this option. Such subscribers tend to keep talk-time to a minimum. Frivolous communication, including dating, happens increasingly through short text messages, which are cheap.

Although China's overall market is a long way from saturation, the lucrative segment of it may not be far off. This is not a total disaster, says Ted Dean, managing director of BDA, since low-yield subscribers also cost less—operators do not need to send prepaid customers any bills, for instance. But it does mean that China's future subscribers will be less profitable than its existing ones. To make matters worse, the regulator has hinted that it intends to give two more licences to mobile operators, perhaps late next year.

The lesson is that China's markets are rarely as good as they seem. Even in mobile phones, there is still a lot of money to be made—Motorola, an American manufacturer of handsets and the top seller in China, for instance, says that it has fatter profit margins there than anywhere else in the world. But investors tend to be carried away by over-optimistic projections of China's markets, and pay over the top to enter them.

China's coastal urban middle classes have been bingeing on everything from life insurance to cars and computers. It is the rural population, however, that makes the Chinese numbers so big, and selling to them is another matter. As foreigners queue up to do business ahead of China's accession to the World Trade Organisation, that is worth bearing in mind.

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Alcohol in Sweden

Loosening up

Aug 30th 2001
From The Economist print edition

European competition law is proving beneficial to Sweden's drinkers

BUYING a bottle of liquor in Sweden is a notoriously disagreeable experience, thanks to years of practice by Systembolaget, the state-owned monopoly retailer of alcoholic drinks. Now this forbidding institution is undergoing a personality change and trying to reinvent itself as customer-friendly. Out go the clinical glass cases in which drink is displayed; in comes self-service. Since July, most stores have started opening on Saturdays.

Behind this revolution is pressure from the European Union. When Sweden joined the EU in 1995, the government gave up its monopoly over the production and distribution of alcohol. It also reluctantly agreed to a gradual repeal by 2004 of the restrictions on imports by travellers.

"Tourist" imports are already undermining Systembolaget's retail monopoly. Students and pensioners in southern Sweden make a tidy living by driving back and forth from Germany and Denmark with boots full of lower-taxed booze. More than 20% of all alcohol consumed in Sweden is imported in this way, a flow that is expected to swell further when the remaining restrictions are phased out.

To prepare for this, Systembolaget announced a restructuring in early August. The move to self-service will allow it gradually to reduce its workforce by up to 30%. It also plans to slash its famously wide selection of wines. Pruning the product range should reduce inventory costs and allow price reductions for the remainder.

Prices at the top of Systembolaget's product range are already competitive. As one of the world's largest buyers, it has long been able to negotiate large bulk discounts, especially on fine wines—so much so that visiting tourists from France often hunt for vintage bargains. Locals suggest that recent investigations of Systembolaget's procurement practices by the European Commission were motivated by a desire to stop it driving such hard bargains with French and Spanish wine producers.

According to a recent opinion poll, Swedes are evenly split on whether Systembolaget should keep its monopoly. But Swedish alcohol consumption is rapidly rising, albeit from the lowest level in the EU. Fears of damaging health effects and alcohol-related crimes are widespread. Swedes have traditionally used alcoholic drinks not so much as a dinner refinement, but to get drunk. Since Viking times, the consequences have often been violent.

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Cisco

A kid no more

Aug 30th 2001 | SAN FRANCISCO
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Can Cisco ever again recapture the dazzle of its brilliant youth?

MANAGEMENT shake-ups are a tricky business. They are most necessary when sales are plunging, but at such times they can easily make things worse. That was the dilemma faced by Cisco, the battered networking giant, when it announced, on August 23rd, its most important management shake-up in four years, aimed mainly at centralising its engineering and marketing.

AP

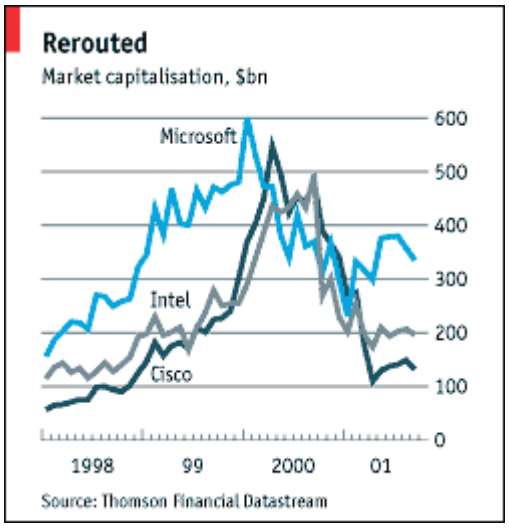
Chambers faces the flood

The timing of the reorganisation might be right because the trough appears to be near. After a dramatic drop in recent months, Cisco's business is stabilising, according to John Chambers, its chief executive. But the Silicon Valley company still has a long way to go if it is to achieve its self-imposed growth target of 30-50% a year once the networking industry recovers from its slump. Can it ever recapture the dazzle and status that it had as the *wunderkind* of the "new economy"?

For *wunderkind* it certainly was. It built most of the engines (80%, according to some estimates) for the Internet revolution: souped-up computers called routers that guide data through networks. But the firm was admired not only for what it did, but for how it did it. Cisco was almost boringly perfect. It mastered the art of serial acquisitions and outsourced all the dirty work to contract manufacturers.

Small wonder that its share price seemed to know no limits. On March 27th 2000, the firm's market capitalisation reached $548 billion, making it briefly the most valuable company in the world (see chart). That increased the shock when the company hit the wall. On April 16th this year, it announced that sales in its next quarter would fall by almost one-third, and that it would lay off 8,500 employees, 17% of its workforce. Cisco, Mr Chambers said, had been hit by a once-a-century flood: "We never built models to anticipate anything of this magnitude."

Cisco's big competitors, such as Nortel and Lucent, are admittedly in much worse shape. Yet some of Cisco's woes appear to be home-made. Having become addicted to growth rates of 60% and more, its management apparently had a hard time finding the brakes. "If you don't believe that it is going to rain, it takes a lot of rain to convince you," says Paul Johnson, an analyst with Robertson Stephens, an investment bank, who is a long-time Cisco watcher.



To be sure, without its much-vaunted internal information systems, Cisco's wounds would be much deeper. Larry Carter, its chief financial officer, probably has access to more information on his PC than any of his rivals at other big companies. But his "cockpit" is no crystal ball. Cisco's management appears to have relied too much on its own numbers, ignoring external warning signs. In early December last year, Mr Chambers still saw an opportunity for his firm to "break away" from its competitors, even though many of its telecoms customers were already in serious financial trouble.

Nor was the famous supply chain as responsive as it might have been. Technology and outsourcing have

made supply chains more efficient, but also longer, which means they cannot be switched off immediately. There is always a lot of material in the pipeline, some of it going from America to Asia and back again.

What made things worse in Cisco's case was that it had, in the summer of 2000, aggressively ordered components so as to cut down on its lead times, which had reached 15 weeks for some products. The firm thus found itself saddled with a huge inventory of parts, of which it had to write off a whopping $2.5 billion-worth.

Analysts are also increasingly questioning Cisco's ability in one of its trademark fields: the serial acquisition of other start-ups. Has its takeover of 73 companies since 1993 really been the unmitigated success it is often claimed to be? The first acquisitions, such as Crescendo Communications, were certainly winners. But Cisco did not in every case manage the trick of buying good technology and getting its legendary sales force to market it successfully. The company has just cancelled a networking product developed by Monterey Networks, a start-up that it bought as recently as 1999 (for $501m), because the gear was "ahead of its time".

Cisco did not in every case manage the trick of buying good technology and marketing it successfully

In any event, Cisco will find it difficult to be as acquisitive as in the past, at least in the foreseeable future. So far this year, it has bought only two companies, Allegro Systems and AuroraNetics (after buying 23 in 2000). The crop is thin partly because venture capitalists are financing far fewer suitable start-ups, but also because Cisco is far less attractive as an acquirer. Its shares are no longer the top currency that they once were. Many leading engineers and entrepreneurs now see the company as a bureaucratic behemoth.

Tornados to tame

Acquisitions will remain an important part of Cisco's strategy, the company says, even if that means paying cash, of which it has plenty. But its restructuring programme suggests that it intends to make its own internal research and development effort more efficient—something that its critics have often advised.

Until now, the firm was divided into three units focusing on different types of customer: big companies, small businesses and telecoms carriers. This set-up had the disadvantage that the units often duplicated efforts on the same technology. Now there will be 11 groups, each in charge of one key area—such as wireless networks, optical equipment or storage.

Getting more bang for its R&D bucks is not the main rationale for the shake-up, says Mario Mazzola, Cisco's new chief development officer, who will oversee the new groups. The changes are more a reaction to customer demand, he says. When Cisco created its present structure in April 1997, different types of customer wanted to build different networks. Now their requirements are increasingly the same; all want to create seamless networks built on Internet technologies.

The new set-up, Cisco hopes, will make it possible to achieve its ambitious 30-50% growth targets. The structure is supposed to allow the firm to focus better on the areas that it has identified as "tornado" markets—which it expects to grow just as rapidly as its traditional router business. The company has identified six such markets, including systems to deliver digital content intelligently over the network, wireless gear for home and offices, and fibre-optic equipment, in particular for networks in metropolitan areas.

Analysts remain sceptical. It is hard to grow that quickly if you are as big as Cisco, which generated revenues of $22.3 billion in its latest fiscal year. What is more, the growth target also presumes that the firm will dominate these tornado markets, and that its core business will continue to expand rapidly, neither of which can be taken for granted. Between 15% and 20% would, analysts suggest, be a more realistic growth target. But Cisco's management insists on the higher figures (although Mr Chambers recently qualified them as a "stretch goal"). Make no mistake, though, even a slower-growing Cisco will remain a formidable company.

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Juniper Networks

Spot the difference

Aug 30th 2001 | SAN FRANCISCO
From The Economist print edition

Cisco's cautious competitor is no clone

FOR most of the American business press it is a simple upstart v incumbent tale: the nimble Juniper Networks is after Cisco, the juggernaut of networking systems. But ask Scott Kriens, Juniper's chief executive, about that casting and he rolls his eyes as if to say, "Stop comparing apples with pears".

In part, Mr Kriens's reaction is a wise business tactic. Many a challenger has trumpeted too loudly, only to be crushed by the incumbent. Juniper is a serious competitive threat to Cisco in the strategic market of high-end routers, the traffic cops of the Internet backbone. But it is also true that the companies are quite different beasts.

Take history. Cisco came into existence almost by accident. Silicon Valley's Stanford University did not want to market the routers developed by two of its engineers, so they went on to launch their own company in 1984. Juniper, on the other hand, was founded in 1996 in a deliberate effort by Pradeep Sindhu, a former Xerox engineer, to create a killer router company.

The chief executives are also an interesting study in opposites. Cisco's John Chambers loves to talk about the networked economy of tomorrow, with everything connected by high-speed pipes. Mr Kriens, by contrast, has a keen interest in economic history. This explains why he is not all that fazed by the current telecoms slump. Yes, there is a bandwidth glut, but prices will drop and demand will rise—just as it did after the railway boom in the 19th century.

What mainly separates the two firms, though, is their approach to the networking business. Cisco has become, through acquisition, a highly diversified company. Juniper has focused on one business: selling home-grown, high-end routers to Internet service providers. The focus has allowed it to grow as fast as Cisco did in its early days; its net revenues in the first half of 2001 were over $500m. It has grabbed a 34.7% share of its market, compared with Cisco's 60.3%, according to the Dell'Oro market-research group.

But putting all its eggs in one basket also makes Juniper vulnerable. It has already begun losing market share—to Cisco, and also to newer competitors such as Avici Systems. In the long run, it will be forced to find new sources of growth. For now, its progress is more or less confined by the increase in Internet traffic (which is still impressive despite the tech slump). It would come as no surprise if, one day, Juniper moved into adjacent markets such as metropolitan networks or optical gear. But if it does, it will do so cautiously. Do not expect it to become another Cisco.

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Face value

India's fermentation queen

Aug 30th 2001
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Kiran Mazumdar Shaw is at the forefront of India's booming biotechnology business

IF INDIAN biotechnology has a cover girl, it is Kiran Mazumdar Shaw, a voluble 48-year-old who owns Biocon, the country's biggest biotechnology company. At the moment biotech is the leading candidate to take over from information technology as India's high-tech star. Or so conferences and magazine covers have proclaimed for months. This week comes the news that two Indian laboratories are among only ten in the world with embryonic stem cells that can be used for research funded by the American government. The hype could soon become hysteria.

Mrs Mazumdar Shaw is not losing her head. Biotech is a “huge opportunity”, she concedes, but “I am concerned about a lot of the hype.” Instant fortunes and annual growth rates of more than 50%, feats that Indians learnt to think of as the norm during IT's headiest days, are unlikely in biotech.

To illustrate why, Mrs Mazumdar Shaw hands over a slip of paper rating biotech against IT on a dozen attributes. Only one of the 12 weighs in favour of biotech enterprises (barriers to entry are higher than in IT). One is mixed news (the costs of invention are higher, but so are the returns). The remaining ten, including the level of investment needed, the time required to develop products and the size of the market, stack up against biotech firms.

Mrs Mazumdar Shaw's sobriety may owe something to her background. Unlike many high-tech entrepreneurs, who plunge into business with little more than a doctorate and a dream, she has been plugging away for two decades with a master's degree in brewing. She soon found that opportunities for brewmistresses in India were few, but that the uses of fermentation are many. Passing up a chance to brew beer in Britain, she formed a joint venture in 1978 with an Irish company called Biocon to manufacture enzymes for packaged fruit juices.

Bio degraded
Biotech market in India, $m

	2000	2005*
Animal & health-care products		
Vaccines	150	300
Antibiotics	225	275
Other	200	350
Agricultural products		
High-yielding & genetically modified seeds	450	650
Other	100	200
Industrial products		
Industrial enzymes	50	100
Amino acids, organic acids	150	200
Yeast and yeast products	150	250
Total	**1,475**	**2,325**

Source: Biocon India *Forecast

Now the Bangalore-based Biocon (the Irish partner has disappeared into a multinational's maw) claims a quarter of the world market for pectinase, an enzyme that breaks down the pectin in fruit juice. In its latest fiscal year, it reported net profits of about $8m on sales of $52m. An initial offering of shares to the public, much hoped for by Bangalore's biotech fans, may happen in 2002.

Mrs Mazumdar Shaw does not intend to be sidelined into low-tech products just because she is in India. Biocon claims to be the first company to get approval in America to use solid-state fermentation for manufacturing statins, a group of cholesterol-lowering drugs. This has enabled it to branch out into high-growth pharmaceuticals, whose sales are now more than twice those of its enzymes.

Biocon has also come up with a “hybrid reactor”, which combines the low cost of solid-state fermentation with the virtues of the (alternative) submerged process, such as better-controlled feeding of organisms. The contraption, which makes it easier to contain organisms and to extract what they produce, will help Biocon to graduate from novel processes to new drug products, such as genetically engineered anti-infectives. A company has been set up to test India's oversupply of sick people for “biomarkers”,

indicators of disease that can be read as early warnings. It is also cataloguing India's rich collection of micro-organisms.

What's brewing

There is much to tempt would-be Biocons into the market. India has more than its share of problems that biotechnology could fix (diseases and harsh conditions for crops, for example) and a wealth of organisms that might be tweaked genetically to do the fixing. Some 20,000 Indians a year gain master's degrees in biology-related disciplines, guesses Mrs Mazumdar Shaw. Like their software cousins, they are potentially available at low cost to western clients. The services on offer, in biotech's case, include research done on contract for others and “bioinformatics”, using computers to make sense of biological data.

However, the industry is still small. Mrs Mazumdar Shaw estimates the market's size at $1.5 billion, including imports. Ernst & Young, a consultancy, puts the number of participants (including government labs) at 800 and the size of the market at $2.5 billion, but that counts people simply making alcohol. A mere 30 companies, it says, are in “modern biotech”, and their sales are a small fraction of the total.

They include vaccine makers such as Shantha Biotechnics and Bharat Biotech of Hyderabad (Bangalore's rival for high-tech glory), as well as pharmaceutical companies such as Wockhardt and Dr Reddy's Labs, which see biotech as a way for India to end its dependence on re-engineering the rich world's drugs and to start inventing its own. The biotech arm of Reliance, a petrochemical giant, is one of the labs with stem-cell lines approved by the American government.

India is now sprouting biotech start-ups that aim to match its silicon exploits. But progress is, as ever, hindered by regulatory backwardness. The country has yet to approve its first genetically modified food, or even its first large-scale trials of genetically modified crops. Nor will it have protection for product patents until 2005 (though it does protect processes).

A push is on to make faster progress. A plant varieties bill, recently passed by parliament, protects novel crops, and permission is expected soon for the first large trials of a genetically modified crop. A proposal for regulatory streamlining, drafted in part by Mrs Mazumdar Shaw, has been presented to the government and, she expects, will be adopted within six months. Biotech may not create as many instant billionaires as IT, but its fizz could be made to last a lot longer.

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Hedge funds

The latest bubble?

Aug 30th 2001 | NEW YORK
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Even if it proves not to be a bubble, the craze for hedge funds is destined to leave many investors disappointed

Get article background

NEVER have hedge funds been more popular. In the first half of this year, almost twice as much money flowed into them as in the whole of 2000. Worldwide, there are now reckoned to be over 6,000 such funds, controlling assets worth over $500 billion.

Hedge funds were not so long ago the preserve of a wealthy few. Now everybody wants to get into them, from institutional investors to the "mass affluent": individuals with as little as $10,000 to punt. In Belgium, hedge funds are advertised on television. In America, where such advertising is banned, hedge funds are still keenly marketed in private, in seminars given by stockbrokers and private banks. To be a hedge-fund manager has cachet.

Is this boom in hedge funds a good thing? Some people reckon that the industry is simply coming of age: it is growing more sophisticated as it acquires a track record that looks more appealing to investors each time that other asset classes—from shares to venture capital—suffer yet another fall. And for all the rapid growth in hedge funds, the scope for more remains. Only one in five "high net-worth" individuals now invests in any form of private equity (which includes venture capital as well as hedge funds). Moreover, it is claimed, both investment quality and risk controls are improving fast.

Others are more sceptical. They point to the many hedge funds of doubtful quality, with inexperienced managers or even charlatans at the helm. Funds are being pushed on investors who do not understand the risks. Anyway, they are hard to monitor and vulnerable to fraud. With performance fees for hedge-fund managers typically soaking up 20% of any annual increase in value, incentives tilt in the direction of excessive risk-taking. (There is usually no penalty should a fund's value fall, and a manager can always wind down his fund and start again.) And as more money goes into hedge funds, it chases a dwindling pool of truly talented managers and sound investment opportunities.

The party-poopers are led by Barton Biggs of Morgan Stanley, a veteran investment strategist and bubble-spotter. "The hedge-fund mania" in both America and Europe, he says, bears all the signs of a classic bubble: "I am sure that many new funds will explode, and their investors will lose a lot of money." This analysis has not pleased some of his colleagues at Morgan Stanley, which is equalled only by Goldman Sachs in its enthusiasm for hedge funds, touting "opportunities" to wealthy customers and supplying "prime brokerage" services to funds. Paul Roye, director of the investment-management division at the Securities and Exchange Commission, advises investors to "be cautious about the hedge-fund craze".

Is there really a bubble in hedge funds? Certainly, a lot of investors have looked at hedge funds only because they are the latest fad. Also, investors tend to chase the best past performers rather than to question whether previous success says anything about future prospects.

Consider "merger-arbitrage" funds, which bet on movements in the share prices of firms that have announced mergers but not yet completed them. According to Meredith Jones of Van Hedge Funds, a

research group, these funds shone last year, generating gains of as much as 17.1%. They have since attracted much fresh money. Yet this year they are up only 4.9%. Many funds lost a packet betting on the merger of GE and Honeywell that European regulators eventually blocked. Now, a lot of new money is chasing funds with a three-year track record, average annual returns of 12-15%, and low volatility: meaning fewer than 250 out of the 6,000 hedge funds, according to Ms Jones.

There are so many different sorts of hedge fund that it is hard to talk seriously about a generalised bubble. For a start, around half of all hedge funds are “long-short equity” investors—just like the original hedge fund, formed in 1949 by Alfred Winslow Jones, who sought to reduce risk by owning some shares while short-selling others. There is no shortage of equities for long-short funds to bet on, and the amounts invested by hedge funds are dwarfed by equity mutual funds. Thus, says Nicola Meaden of Tremont/TASS, a research firm, there is no need to worry about the flood of new money causing a bubble in the underlying assets.

This may not be so true for “relative value” hedge funds, which try to arbitrage away differences in the prices of two assets that have essentially identical economic characteristics—a Treasury bond with 30 years to maturity, for instance, against one that matures in 29 years. Here, the hedge funds gain by correcting the mispricing of assets. But there is a limit to the gains from this form of arbitrage. According to Will Goetzmann, an economist at Yale, a broadly fixed amount of dollars is available from the strategy, rather than a fixed rate of return. More money flowing into the strategy will mostly reduce the average rate of return to investors. And to compensate for smaller average returns, funds may be tempted to multiply their stake by borrowing more money, increasing their risk.

The inflationary impact of fresh demand is cut a bit because plenty of established hedge funds have closed their doors to new investors. Eventually, however, many hedge funds succumb to the temptation of growing too big. At that point, they find it harder to invest money without the rest of the market turning against their positions. And they often suffer managerial problems as their staff expands. Either way, returns fall.

Much new money flowing into hedge funds, particularly from pension funds, is coming with demands attached—notably for greater transparency, and for evidence that risks are well managed. There is also growing interest in more rigorous performance analysis, including that relative to benchmark indices (see article). If returns disappoint, there may be growing pressure to cut fees—which would be a sure signal that the industry is maturing. At present, some charges are actually rising: there are funds with performance fees of 50%, which smacks of bubbledom.

Bubble or no, there is every chance that hedge funds will perform less well in future than in the recent past. Indeed, although it is taken on trust that hedge funds outperform in a bear market, there is little evidence for this. Hedge funds did so poorly during the bear market of the 1970s, with many going out of business, that the great Winslow Jones himself was moved to observe that “the hedge fund doesn’t have a terrific future”.

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Hedge funds with listings

Martyrs to transparency

Aug 30th 2001
From The Economist print edition

A listed hedge fund sounds like an oxymoron

Get article background

INVESTORS and regulators may clamour for more transparency from hedge funds. But that is not, it seems, what the market is hearing. PlusFunds.com, based in New York, has tried to encourage transparency in hedge funds by persuading some new ones to list on the Bermuda stock exchange, requiring them to post daily asset values. Three years on, only 18 funds are listed, accounting for around $500m-worth of assets. Traders are sceptical that PlusFunds's valuations are meaningful, given the often illiquid instruments—such as derivatives or distressed debt and equity—in which many hedge funds invest.

PlusFunds, whose shareholders include J.P. Morgan Chase, Merrill Lynch and Credit Suisse, is undaunted, but it is planning to loosen its stringent listing rules. Instead of taking only new funds, it plans to list existing funds, provided that it can "tunnel" into the right kind of data to produce a net asset value, affirmed daily by Standard & Poor's (S&P), a rating agency. PlusFunds may also become yet another provider of a hedge-fund index—though with the additional credibility of S&P.

In a further effort to expand, PlusFunds will make its sophisticated—some say too sophisticated—valuation system available to another champion of transparency, Albourne Partners in London. Albourne advises investors, including pension funds, on which hedge funds to choose. To avoid conflicts of interest, it runs no investment funds itself; nor does it invest in them.

Instead, it looks at the risk management of hedge funds and at the integrity of managers—although it also advises on the sale of partnerships in hedge-fund firms. In theory, PlusFunds and Albourne are a good fit, so long as customers can stomach the wacky "alternativeness" of Albourne's website. There you will find a virtual village in which hedge-fund junkies can visit shops, run by some of the usual suspects—Barclays, CSFB, Merrill Lynch or UBS—or drop in for gossip at the Bridge Inn. The beer, of course, is crystal clear.

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Measuring hedge funds

The benchmarking bane

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Hedge-fund managers don't like indices, which are proliferating

ATTEMPTS to establish hedge-fund indices as benchmarks for a fledgling industry are fraught with theological conundrums. Hedge-fund indices might track the performance of the entire hedge-fund "universe", for instance; or just groupings of hedge funds that employ apparently similar investment strategies. Yet even there, hedge funds that exploit, say, valuation discrepancies among different classes of company securities are hard to compare, so varied are the possible strategies.

Moreover, one of the few common characteristics of hedge funds is their aristocratic focus on "absolute" returns: the notion that you can make money even if there is a bear market in stocks or bonds. "Benchmarks were the reason why I left traditional money management," sniffs Richard Chenevix-Trench, a hedge-fund manager at Sloane Robinson.

Yet benchmarks provide a semblance of security that is crucially important to institutional investors responsible for other people's money. "I look for relative returns, transparency and an investment process," says Mark Anson, chief investment officer of CalPERS, the pension fund for California's public-sector workers, which manages $156 billion. Relative returns help to put a fund manager's success or failure into context—no bad thing when wild claims about performance are made.

Institutional investors, including Mr Anson, acknowledge the difficulties of producing a meaningful index. Yet they insist on benchmarks as a permanent feature of institutional portfolios. CSFB/Tremont, Hedge Fund Research, Standard & Poor's and others are already catering to the demand, by publishing indices. Zurich Capital Markets recently launched its own series. Morgan Stanley Capital International, the market leader for stockmarket indices, and Financial Risk Management, a hedge-fund research firm, are putting finishing touches to their planned indices.

"It is all highly confusing," says Simon Hopkins at Global Fund Analysis, a hedge-fund consultancy. Each index provider produces sub-indices for every strategy with dissimilar outcomes. They apply differing criteria for including a hedge fund in an index: some weight funds equally, others according to size. And, parochially, they tend to focus on America, largely ignoring hedge funds in Europe and Asia.

Life is further complicated because many funds are not regular reporters of performance, while others switch from one hot investment strategy to another. Even two hedge funds that appear similar—for instance, both may take long and short positions in European equities—may have different risk profiles. One might be highly leveraged, taking big positions in "growth" stocks, while the other might be taking smaller positions in "value" stocks.

More fundamentally, some indices include hedge funds that are closed to new business. Should index providers create separate indices for investable and for closed hedge funds? The industry is years away from accepted standards for benchmarking, Mr Anson concedes.

Nevertheless, competition to establish a leading index and to create tradable products related to it will only increase. On August 30th CSFB was due to go live with an internal fund built to replicate the CSFB/Tremont hedge-fund index—even though some of the 374 funds in the index are closed to further investment. CSFB says that, if the in-house fund of $50m-100m is successful, the firm will launch a public one in October. Pre-empting CSFB, Global Investment Advisors in London has launched a "fund of funds"—minimum investment $10,000—to track the CSFB/Tremont index. It says it will buy into closed funds, if necessary "through contacts in the secondary market". After tradable index funds, surely a derivative cannot be far away. Next up: a hedge-fund future listed in London or Chicago?

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Monetary policy in the euro area

The ECB decides

Aug 30th 2001 | FRANKFURT
From The Economist print edition

Europe's central bank has cut interest rates, at last

AFTER a summer pause, the motley crew of economists, hacks and bankers who watch the European Central Bank were back on the trail this week. On August 30th, a big day for the ECB (see article), interest rates were cut by a quarter-point, to 4.25%. Except for one earlier quarter-point trim in May, the ECB has generally resisted pressures for rate cuts all year, in the teeth of growing evidence that the euro area's economies have been slowing sharply. Despite the central bank's past caution, quite a few economists had expected a cut this time.

An indirect reason for this has been a further run of statistics that showed a weakening euro-area economy: German GDP was flat in the second quarter, for instance, and the Italian economy shrank a little. Across the euro area as a whole, it seems unlikely that GDP grew much, if at all.

Only an indirect reason? Yes, because the ECB targets not economic activity but inflation: its goal is to keep inflation below 2%. With economic growth weak, price pressures should ease. However, there has also been direct evidence that inflation, 2.8% in July, is subsiding, and should head back towards the ECB's target in the months to come. For instance, German producer prices and import prices both fell in July.

Was there any reason to wait a few weeks more and see? Not really, even though broad-money growth in the euro area (to which the ECB attaches a special role) accelerated in July. The three-month average of annual broad-money growth rose from 5.3% to 5.9%: even after stripping out acknowledged distortions, that is above the bank's target of 4.5%. The ECB itself had said that a prime cause was a shift into short-term bank deposits, thanks to a flat yield curve and weak stockmarkets. This looks an unlikely source of consumer spending—and hence of inflationary fuel.

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Euro notes

Unveiled

Aug 30th 2001 | BRUSSELS AND FRANKFURT
From The Economist print edition

The euro area's new banknotes are ready. But are Europeans?

IN ONLY four months' time 300m people in 12 European countries will ditch their old banknotes for crisp, new euros. For some time, Europeans should have known (if they could be bothered to find out) that the new notes will carry pictures of bridges. To avoid favouring individual countries, these represent architectural styles rather than actual structures—although the French are pretty sure that the *euro*5 note shows the Pont du Gard.

AP

Letting the notes out of the bag

On August 30th, the notes were unveiled in detail for the first time, in the proper sizes and colours, and complete with various "security features". A historic event, trumpeted the European Central Bank, which deemed its press conference worthy of the Frankfurt opera house rather than its own tower a few yards away. The ECB also trailed new television and newspaper adverts for the currency: Europeans can expect a heavy bombardment as the changeover draws near.

The central bank will be hoping that it has got its timing right. It has held the final designs back until now, to minimise the risk of counterfeiting. For the same reason, it says, it will not allow notes to be handed out to ordinary people until January 1st, when they become legal tender—although deliveries to banks and thence to security firms and retailers are due to start in some countries on September 1st. The ECB has resisted calls from the European Parliament for the public to have low-value notes in December. The parliamentarians wonder, reasonably, whether a few days would help forgers that much. They think that getting people used to the new money would be a good defence against duds.

Some think that the creation of a cross-border currency, with high-denomination notes worth *euro*500 ($455), will be a gift to organised crime. Against that, the notes should embody printers' latest anti-forgery techniques. Thanks to technical advances, says Gerhard Bereswill of the Hesse state police (in whose bailiwick Frankfurt lies), the new notes should be harder to forge than D-marks or other national currencies. In any case, he adds, the game between the authorities and forgers will not begin properly until the notes are in circulation.

Getting people to recognise the notes, though, is only part of the problem for the next few months. This year a host of scary scenarios have been sketched by journalists, academics and consultants who believe that the euro area is hopelessly ill-prepared and heading for chaos. The doomsters worry that retailers with two lots of cash in their tills will be sitting targets for armed robbers; queues at shops and railway stations will reach gargantuan lengths as shoppers and shop assistants flounder in confusion; and bank machines will not be converted to euros in time, or will run out of notes.

Although this looks vastly overdone, there is certainly scope for trouble, or at least confusion. The richest countries are not necessarily the least at risk. Germans, for example, are still relatively heavy users of cash and so may be more likely to suffer delays at check-outs. In France, only 1% of credit-card transactions were in euros in July, far short of the 70% that the government hopes for by November.

Optimists and pessimists can easily find favourable statistics. On the one hand, only one person in five knows the exact (well, six-digit) value of the euro in national-currency terms; on the other, most know it roughly. According to a Eurobarometer poll in the spring, only 53% of Germans support the euro (fewer than half in the east); yet 83% of Italians are eager to knock a few noughts off the money in their pocket. Around 90% of Belgians know that they will be able to use euros throughout the euro area (tick);

but 60%, in line with the euro-area average, expect to be able to use it in the remaining three European Union countries (don't try it in Chingford, Hercule).

The sensible money says that things will probably be all right on the day. Four months of advertising to come ought to make some difference. Hitherto, most Europeans have not had to think in euros. But in a few months, they will have to adapt quickly—and so they probably will.

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Poland's changing capital markets

Patriotic pensions

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The rise of pension funds helps a weak stockmarket

WITH a budget crisis looming, a finance minister sacked this week and more emerging-market jitters, Poland's economy is looking decidedly febrile. A falling stockmarket has deterred western investors, and the opposition ex-Communists look set to win a big majority in next month's parliamentary elections. Through all this, Marcin Krupa, a director at Poland's pensions watchdog, UNFE, is a contrarian. He says things have changed since the Russian financial turmoil three years ago this month: domestic pension funds are a point of stability in the country's wobbly capital markets.

AP

East, west, home's best

Two years ago the government licensed 21 privately managed pension funds, hoping that they would defuse a potential demographic time-bomb. Based on Chile's heavily regulated model, a three-tiered pension system was introduced, melding the state-run, pay-as-you-go scheme with a compulsory private savings plan for all new entrants into the labour market, and also for all aged under 30 at the end of 1999.

Though the reforms are recent, fully 10.5m Poles have signed up for private pensions, exceeding the government's wildest expectations. While a foul-up in transferring contributions to the funds has yet to be sorted out, a recent report by UBS Warburg, an investment bank, extolled the Polish pension system as "a benchmark for many euro-zone economies to aspire to". Particularly impressive is the funds' freedom to invest up to 40% of their portfolios in domestic equities (the rest is parked mainly in government bonds).

Even in today's bear market, the funds hold nearly a third of their $3.5 billion under management in Polish shares. That provides a steady flow of institutional cash to an erratic stockmarket that had, until a few years ago, seen foreign portfolio investors calling most of the shots. Polish pension-fund investments today account for roughly 10% of the free float on the Warsaw bourse. That could reach 40% by 2004 if the funds maintain their current 25-30% equity weighting.

All the more reason, say the funds, for the government to lift their 5% cap on foreign investments, lest the funds outgrow the local bourse—especially given the present dearth of public offerings and privatisation opportunities. The OECD recently argued that the 5% limit breaks laws on the free movement of capital and should be revised upwards. The government's rejoinder is that its private pensions are not voluntary schemes in the Anglo-Saxon mould. Rather, they are compulsory, state-backed plans that guarantee minimum rates of return.

Stick-at-homes

The pensions watchdog, with the government's support, is wary of the funds dabbling in foreign assets, fearing big losses and possible damage to confidence in private provision. It believes that there is plenty of investing to be done at home before the funds shift assets to more tempting places. This at least sounds patriotic, even if it is not sound economics.

For the majority of pension funds, in any case, this is hardly an issue: they are too small and inexperienced to contemplate investing abroad. But the "big four", Commercial Union, ING's Nationale-Nederlanden, AIG and Poland's dominant insurer PZU, chafe at UNFE's restrictions. Together, they account for over 70% of total pension-fund assets and have the global networks to target foreign

stockmarkets.

The flag-waving seems to be paying off in some respects, at least. It is, most notably, helping to improve shoddy domestic corporate governance. Several pension funds have brought errant managers to task, especially in smaller companies on the Warsaw bourse, in which they have amassed sizeable stakes. Yet UNFE frowns on overbearing shareholders. It threatens to reduce the maximum stake a fund may hold in a listed company.

Rights for minority shareholders in Poland have certainly got more attention since the funds started to pour money into stocks: a number of high-profile corporate battles over the past few months were triggered by assertive pension funds. But pension funds need more listed companies to invest in, and less dominance of minority shareholders by “strategic” investors. Otherwise who can blame them for casting their eyes abroad?

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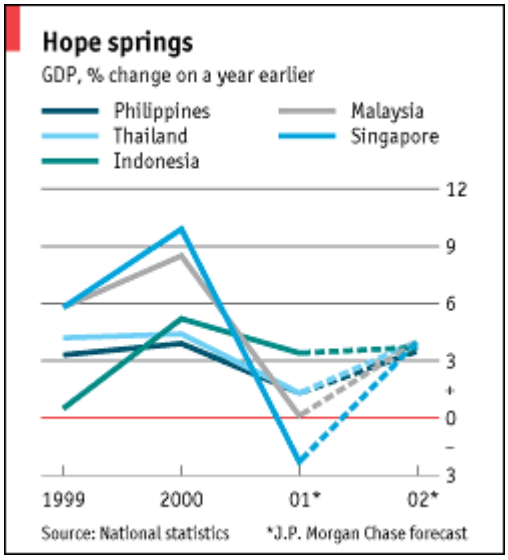
South-East Asia's economies

Stable but sickly

Aug 30th 2001 | BANGKOK AND SINGAPORE
From The Economist print edition

Now that political fires are out, attention turns to economies

NOT a celebration, sure, but it was still an upbeat parade. Last week, leaders from three troubled economies—Indonesia, Thailand and the Philippines—paid successive visits to Singapore in order to boost their image and drum up investment. Their visits served notice that a large chunk of South-East Asia has stabilised, as far as politics is concerned: for much of the previous year, elections, impeachments and indictments had made the region seem hopeless. As currencies and stockmarkets in the three "mango republics" fell, the more stable (and more developed) countries of Malaysia and Singapore were tainted by association. Now, just as its economies run bang into a global slowdown, South-East Asia seems to have put the biggest of its political problems behind it. But will that help its economies?



There is little the region's governments can do about the worldwide slump in export demand. Exports by South-East Asia's five biggest economies actually fell in the first half of this year, by 1.5% compared with a year earlier. Since exports to America and Japan account for over one-quarter of the group's GDP, efforts to offset the shortfall can do only so much.

Consider Singapore's economy, which is geared towards trade, property and financial services. Its GDP fell at an annual rate of 10.7% in the second quarter, and global lay-offs by American and Japanese firms could send its unemployment rate above 4% by the end of this year. Since Singapore is financially sound, however, as well as politically stable, the government is sticking to its long-term economic plans. Rather than approve pointless new infrastructure projects, it is promoting bank mergers, fresh job losses notwithstanding.

But then geography is one of the few things that Singapore shares with the rest of South-East Asia. Its emerging neighbours face not just a global slowdown, but also high corporate debts, stalled bank lending and wary foreign businessmen, as well as a host of structural problems. If it helps to bolster confidence at all, therefore, a little more stability in those countries could prop up consumption and investment during the export downturn.

The most dramatic change has occurred in Indonesia, where Megawati Sukarnoputri became president when her predecessor was impeached on July 23rd. After three years of histrionics, Jakarta is calm and confidence is rising. Miss Megawati has stocked her new economics team with professionals, and is unlikely to shuffle them as frequently as did her predecessor. The rupiah is still more than 10% higher, despite some slippage, than when she took office.

Thanks to the change of cast, a team from the International Monetary Fund signed an updated agreement with the government on August 27th, with macroeconomic targets far more encouraging than the scenarios of a few months earlier. Indonesia plans to run a fiscal deficit of 3.7% of GDP this year, for example, roughly what it was aiming at before impeachment mayhem clobbered the rupiah. After its board's approval—expected in a week or so—the Fund will release the next $400m instalment of Indonesia's $5 billion aid package, suspended since December. Indonesia should also be able to restructure its loans with Paris Club creditors.

Though far less pronounced, political risk has also fallen sharply in Thailand and the Philippines. But these two young governments now face contrasting sets of problems. Miss Megawati's counterpart in Manila, Gloria Macapagal Arroyo, gained the presidency in January when her predecessor connived his way through a long impeachment trial of his own, only to be forced out by street protests. Coup rumours and street riots then hounded Mrs Arroyo ahead of congressional elections in May. Her country now seems much more stable, though risks remain. Kidnappings, both of large groups in the Muslim south and of wealthy businessmen in the capital, continue to sap confidence; and if the prima donnas in the Senate choose to, they can still make Mrs Arroyo's life difficult.

She has nevertheless taken a firm hand to the economy. In her first seven months, she has consistently held the fiscal deficit below target—perhaps the most important measure by which investors assess her. Between January and July, approvals for new investment rose fivefold, compared with a year earlier. July's production figures suggest that businesses are now confident enough to begin rebuilding inventories. Moreover, although the national accounts have been heavily revised, preliminary data released on August 30th show that the Philippines grew by 3.3% year-on-year.

Contrast that with Thailand, which now seems far more stable than the Philippines, but is squandering its chance to make structural reforms. An indictment by the anti-corruption agency hung over the government of Thaksin Shinawatra from his election in January until August 3rd, when the Constitutional Court narrowly voted to acquit him. He is now free to govern with the largest parliamentary majority in Thailand's history. Yet Mr Thaksin is using that clout to create a raft of new entitlements and public-credit schemes. Sadly, Thailand is beginning to look a little like Malaysia, where the government maintains political stability at all costs, while eschewing needed reforms. Thailand and the Philippines thus offer investors a contrasting choice: plunk your money on the former if you think that stability alone matters more than what governments do with it.

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Economics focus

On target?

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Inflation targeting is all the rage, but this approach to monetary policy does not provide all the answers

CENTRAL bankers are dedicated followers of fashion. This year, countries as diverse as Iceland and Turkey are joining the in-crowd by adopting inflation targets. Since New Zealand pioneered the practice in 1990, it has become ever more popular. By the end of last year, a further 18 countries, from both the developed and developing world—ranging from Britain and Canada to Chile and South Africa—had followed suit.

A new study* of the first decade of inflation targeting shows why the bandwagon is rolling. The regime has proved "a very successful new monetary framework", conclude Frederic Mishkin and Klaus Schmidt-Hebbel. It has helped countries to bring inflation down to levels that would not otherwise have been reached, they argue. In emerging economies, the reduction in inflation has involved a smaller sacrifice in terms of lost output than other policy regimes. In both developed and developing countries, output over time has become less volatile.

But wait: inflation targeting was launched into calm seas. With largely benign economic conditions during the 1990s, sceptics say, the new regime has not really been tested. Not so, respond the two authors. Many countries with inflation targets are small, open economies that suffered big currency devaluations after the Asian crisis of 1997-98. Yet, unlike earlier shocks, this one did not cause inflation to surge.

To a large extent, the virtues of inflation targeting lie in the absence of the vices of other regimes. Unlike exchange-rate commitments, inflation targets are not vulnerable to speculative attacks on the currency. Unlike monetary targets, inflation is a final rather than intermediate goal. That would not matter for monetary targets if there were a direct link between money-supply growth and inflation. Yet this relationship has proved treacherous, mainly because of instability in the demand for money.

By contrast, an explicit inflation target anchors price expectations in a far more straightforward way—by combining a clear, rules-based regime with some tactical discretion by the central bank over how to hit the target. As with the best conjuring tricks, there is some sleight of hand here: inflation targeting depends on credibility. If the central bank can convince the public and the markets that it is utterly committed to its goal, people's expectations will change. Once price-setters and wage-bargainers believe that the central bank means business, monetary policy gains extra clout.

In principle, the same trick should work if the economy is suffering from deflation rather than high inflation. Some Japanese politicians have joined economists in urging the Bank of Japan to adopt an inflation target. They think that the reform would help to loosen the grip of a deflationary mindset. If the Japanese expected prices to rise again, that would enhance the effectiveness of the Bank's monetary policy in overcoming deflation. A look at Sweden's experience with a price-level target in the 1930s suggests that it succeeded in raising inflationary expectations despite fears of deflation.

The spread of inflation targeting has gone hand-in-hand with greater independence for central banks. Credibility, again. The more independent central banks are, the more they are trusted by investors. That allows them to get the financial markets to do more heavy lifting. If the central bank cuts short-term interest rates, investors will no longer counteract the monetary easing by demanding higher rates on long-term bonds, in expectation of rising inflation. But as part of the deal, central banks have had to lift traditional veils of secrecy, to become more open in their operations and better at signalling their intentions to the markets.

Inflation-targeting regimes have a further virtue: they create a framework in which a central bank can be

both independent and democratically accountable. The government can set the goal for inflation while leaving to the operationally independent central bank the task of how to meet that objective. This division of responsibility can reinforce, not diminish, the central bank's authority.

The end of monetary history?

Listen to some advocates of inflation targeting, and you might imagine that they have discovered the holy grail of monetary policy. In fact, the jury is still out on the effectiveness of a regime that has not yet been tested by inflationary shocks like those of the 1970s and 1980s. So far, inflation targeting has locked in low inflation rather than brought about major disinflation. In this respect, Turkey's experience will be a valuable test case, for the annual rate of inflation is forecast to be almost 60% when the new system comes into force later this year.

Furthermore, however desirable it is to secure low inflation, narrowly defined, this cannot be the sole objective of monetary policy. After all, dangerous imbalances can build up in the economy even when inflation as conventionally measured is at bay. There is a strong case for the central bank to take more explicit account of asset prices or of misaligned exchange rates rather than focus only on retail-price inflation.

The point is that there is more to monetary policy than trying to achieve a single policy objective. The solution to this problem of multiple goals is to allow the central bank more discretion. However, that could start to undermine the credibility that underpins a largely rules-based regime. For all its virtues, inflation targeting does not resolve all the problems surrounding monetary policy.

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* "One decade of inflation targeting in the world", by Frederic Mishkin and Klaus Schmidt-Hebbel. National Bureau of Economic Research working paper, July 2001.

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Car design

The old new thing

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Some vehicle technologies from the past are being dusted down for use in the present and the future

SOMETHING is missing in the redesigned Audi A4. Step on the accelerator and the car glides smoothly away without the repeated, jerky interruptions of an automatic transmission shifting gears. That is because Audi has replaced the car's conventional automatic gearbox with a transmission system it calls "Multitronic".

Instead of the normal fixed-ratio gears that are found in automatics and manuals alike, a Multitronic gearbox uses a tightly stretched belt to link two cone-shaped shafts, one connected to the engine, the other to the wheels. By adjusting the position of the belt on the shafts, the engine can run constantly at or near its optimum speed, regardless of load. Indeed, different optima are available, depending on whether a driver wants performance, fuel economy or some intermediate combination of the two.

A great, new idea? Well, yes and no. Great, possibly. New, not exactly. Older readers may remember the DAF "Variomatic" gear box from the 1950s. And the idea of a continuously variable transmission (CVT) is even older than that. The first car to use one was the French-made Fouillaron, in 1900.

In the past, CVT never worked well enough to become the industry standard. But Len Hunt, the head of Audi's American arm, hints that within a few years it may replace conventional automatic transmission in all vehicles bearing the marque. And Audi (or more accurately its owner, Volkswagen) is not alone. General Motors will unveil a CVT on the new Saturn Vue this autumn, and most other manufacturers are considering versions of their own. CVT is thus an extreme example of a more general phenomenon—the revival, using modern techniques, of old designs for car parts that seemed like good ideas at the time, but did not quite work with the technology then available.

Nothing new under the sun

In the case of Audi's Multitronic CVT, the most significant changes are the mechanical properties of the materials used to make the belt, and the electronics that control the transmission. Until now, manufacturers of CVTs have relied on cloth or rubberised belts that could stretch or snap. Instead, Audi has crafted a high-strength metal belt made of more than 1,000 separate but overlapping links. Meanwhile, the system measures a variety of signals, and runs them through a computer algorithm that works out the appropriate gear ratio at any given moment. These signals include engine and vehicle speed, and the angle of depression of the accelerator pedal.

This combination of the mechanical and the electronic is known, inelegantly, as "mechatronics", and it is what is allowing the revival of previously unsuccessful technologies. Another example of mechatronic revival is adjustable suspension. This was first tried in 1933 by Cadillac, when it was dubbed Ride Regulator. A driver could choose five settings between "soft" and "firm" by flicking a switch on the instrument panel. It was not a success.

This autumn, Cadillac plans to introduce the Ride Regulator's modern successor, MR continuously variable

suspension. “MR” refers to the magneto-rheological fluid that fills the vehicle’s shock absorbers. Such a fluid’s viscosity changes dramatically in the presence of a magnetic field, so a car that uses it to smooth out the road can respond within a millisecond or so to changes in the conditions, or to the way the driver is driving. Once again, the decision on what response is appropriate is taken by an algorithm programmed into a specially designed microprocessor. This algorithm looks at signals from the steering wheel and brake pedal, and measures speed and road conditions using sensors located in each wheel. These inputs determine the settings of individual shock absorbers—the actual stiffness being controlled by currents sent to electromagnets in each.

A third technology that is coming round as part of the mechatronic revival is “displacement on demand”—in other words, using only those engine cylinders that are actually necessary to power a car in the conditions that it is experiencing. The first attempt to do this was made more recently than those at continuously variable transmission and suspension—in the mid-1980s, by General Motors. Once again, the firm’s Cadillac marque was the guinea pig. Its cars were fitted with so-called V-8-6-4 engines. In theory, these used all eight cylinders when pushed, but throttled back to six or four when cruising. That way, they would save fuel. In practice, they hiccuped their way to a short production run and were, their inventors hoped, forgotten.

But not by all. Once again, GM’s engineers, spurred on by Dennis Mooney, the company’s executive director for vehicle integration, hope to make displacement on demand work by using a microprocessor to take the pulse of the engine thousands of times a second, and then make adjustments so swiftly and subtly that the driver has no idea how many cylinders are firing at any particular moment. The decision about which cylinders to use is based on factors including the number of revolutions per minute that the engine is turning, the vehicle’s speed, the load it is carrying, and whether it is coasting or accelerating.

How far the trend will continue is unclear, but there is probably scope for more industrial archaeology of this sort. Early car manufacturers, who were making things up as they went along, tried all sorts of ideas before settling on the conventions that are incorporated into modern vehicles. Joysticks, steam engines and chain drives all came and went. Perhaps their times will come again.

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Ageing

Only a matter of time

Aug 30th 2001
From The Economist print edition

Want to live to 100? Inheriting the right genes helps

WHEN Sophie Tucker, a popular singer and vaudeville star, was asked the secret of her longevity, she replied “keep breathing”. New research suggests that the secret may actually be more complicated. It is a matter of having the right genes.

Annibale Puca, of the Howard Hughes Medical Institute in Boston, and his colleagues compared the genetic material of 137 sets of aged siblings to see if they routinely shared particular stretches of DNA. The results, just published in the *Proceedings of the National Academy of Sciences*, suggest that they might. Long-lived siblings frequently have a particular piece of chromosome 4 in common (ie, all the brothers and sisters involved inherited it from the same parent). That suggests this piece of chromosome carries a gene which, when present in a particular version, helps people to live to an exceptionally old age.

Dr Puca’s study is the first to scan the entire genome for such data. Having found a region of interest, though, is only a start. First, the result needs to be confirmed. Linkage studies, as these sorts of investigation are known, have a habit of evaporating under scrutiny. Second, if it is confirmed, the gene (or, possibly, genes) involved must be identified. The draft of the human genome that is now available should make that easier than it would have been a few years ago, but the chromosomal region that Dr Puca has identified still contains several hundred genes that need to be examined.

Even so, mere confirmation would be a significant advance. Researchers have known for years that longevity runs in families, but they have debated how much that is due to genetic influences, and how much to a shared environment. Supporting evidence for a genetic contribution comes from experiments on fruit flies, mice, threadworms and yeast. These show that if such creatures inherit the right genes their lifespans can be extended dramatically. Furthermore, some human genes are already known to contribute in a small way to longevity, protecting against Alzheimer’s disease and heart problems.

Theory also supports the idea that ageing is under genetic control. The “disposable soma” hypothesis suggests that length of life is a balance between the energetic investments that an individual makes in reproduction and in maintenance. However, as Thomas Kirkwood, one of the authors of this hypothesis, and a professor of medicine at the University of Newcastle-upon-Tyne, in England, points out, the hypothesis suggests that ageing is complex, and involves multiple genes—which is not what Dr Puca seems to have found.

Thomas Perls, a professor of medicine at Harvard Medical School, and one of the authors of the study, says the group has its own dose of healthy scepticism. Nevertheless, some of the authors of the study (including Dr Perls) are not so sceptical as to miss out on the opportunity to start their own company—Centagenetix—in order to pursue the matter. One thing in favour of there being only a few genes involved, observes Dr Perls, is the rarity of centenarians: only one in 10,000 people make it. If Centagenetix find longevity genes, he says the firm will patent them.

If a few crucial longevity genes are found, they would certainly be interesting. They could form the basis for research into the cellular pathways that are important to the ageing process. That would give clues about how to slow down ageing in the wider population. Dr Perls speculates that some kinds of disease-resistant genes may be involved—for example, genes that are better at repairing DNA, or genes for metabolic processes that produce rather fewer damaging, oxygen-rich free radicals.

That might explain why what looks to be a big genetic advantage is actually so rare in the population. According to the disposable soma hypothesis, individuals who make a large energetic investment in

maintenance and the ability to fight disease may be compromising their ability to reproduce. This fits with a study Dr Kirkwood did on fertility, family size and lifespans in British aristocrats (for whom good genealogical records are available). Aristocrats with the longest lifespans had smaller families. Furthermore, work he has published in August's *Nature Medicine* suggests a mechanism. Women who have a highly reactive immune system might be better able to fight off infectious diseases but, conversely, be more likely to reject embryos in their wombs (with whom they share only half of their genes) as foreign objects.

If Centagenetix finds the hoped-for genes there is one other issue worth considering. If exceptional longevity is conveyed by only a few genes, these could be tested for in a relatively simple fashion. Some people would then know that their risk of dying young is far lower than average. These individuals would benefit more than the average person from their pensions and less from life insurance.

Life insurance works on the basis that individuals do not know their precise risks of dying. As Steven Haberman, a professor of actuarial science at City University, in London, points out, if somebody retiring at 60 knew that he was likely to live to be 110, barring accidents, he would not want to take out life insurance and subsidise the less long-lived in society. Buying an annuity, however, would give him an income for nearly half his life. So, if there is a precise genetic marker for longevity, insurance companies need to have the same information that an individual has—or they will go bust. Yet, according to Dr Haberman, companies selling annuities take no notice of the risk of their customers living much longer than average.

Dr Perls reckons that it will take about nine months to track down the crucial gene or genes, if it or they exist. In the meantime, Ms Tucker's advice still obtains: do not hold your breath.

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Viral diseases

Good vibrations

Aug 30th 2001
From The Economist print edition

A new technique for detecting viruses works by listening to them

TREATING viral diseases is notoriously hard. One reason is that for many such diseases, the amount of virus in a patient's bloodstream (known as the viral load) has to be monitored carefully in order to work out the appropriate drug dose.

At the moment this is often done by quantitative PCR, which uses an enzyme called polymerase to "amplify" part of a virus's genetic material by repeated duplication, until it is chemically detectable. But quantitative PCR is time-consuming; and in viral diseases time is often of the essence. Now a technique described in *Nature Biotechnology* by Matthew Cooper and his colleagues at Cambridge University may provide that essential time.

Instead of detecting viruses chemically, Dr Cooper listens for them. To do this, he and his colleagues use an apparatus called a quartz crystal microbalance.

The balance is a disc made of a polished quartz crystal, with two electrodes attached to it. Sending an electric current of the right frequency through the quartz causes it to resonate, much as a soprano singing at the proper pitch can shatter a champagne glass. By increasing the voltage—the equivalent of singing louder—the team can make the crystal oscillate more and more violently.

As the vibrations grow, anything attached to the quartz will eventually be thrown off. It is possible to measure exactly how much was initially weighing down the crystal by listening to the sounds of the objects departing, using the crystal itself as a microphone. The extra vibration caused by a departing object generates a current in the quartz, and this can be measured via the electrodes. If the objects in question are virus particles, an estimate of their number can then be made.

The trick is to make the viruses stick to the quartz in the first place. To do this, the team coated it with chromium, gold and mercaptoundecanoic acid. This unlikely combination of chemicals made the quartz, in turn, chemically attractive to antibodies. And, since antibodies can be tweaked so that they stick to one particular sort of virus alone, that means that the quartz can be made virus specific.

To prove their point, Dr Cooper and his colleagues chose a virus called type 1 herpes simplex (HSV1), which causes cold sores. After running a fluid containing HSV1 over the quartz crystal, they were able to measure the presence on it of anything from one to 1m viral particles.

The concentration of the virus in the fluid can then be worked out from the number of viral particles that stick to the quartz. Naturally, this is easier to do with the experimental solution that the team used than with blood, saliva or other bodily fluids. So far, HSV1 samples diluted in calf serum, to mimic such real-life samples, give a signal that is only a quarter of that from the original test fluid. Dr Cooper thinks this is because proteins in the serum are blocking some of the binding sites on the crystal. Yet even when the waters are muddied with serum, a discernible signal emerges. So, once the system is refined, the group expects to be able to detect and quantify viral load from clinical samples.

The researchers are now trying to develop their discovery into a practical, portable device. Success would make for a big improvement in the treatment of diseases that are frustrating to deal with today.

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Mimicry

On the other seven hands

Aug 30th 2001
From The Economist print edition

This octopus is a great impersonator

MANY animal species mimic others that are poisonous, venomous or just plain ornery, to discourage predators from having a go at them. Some have mimicry down to such a fine art that different individuals mimic different models, reducing the chance that a predator will realise it is being systematically fooled. But no animal has drawn the logical Darwinian conclusion, and evolved a way for a single individual to mimic several different models, according to circumstances. Or so it seemed until Mark Norman of the University of Melbourne and his colleagues discovered the “mimic octopus”.

Octopuses have two characteristics that ought to make them naturally good mimics: their bodies are flexible, and can thus take on different shapes, and their skins are covered with pigment-filled cells called chromatophores that can expand and contract almost instantly, and thus change the creature’s surface pattern. The latter trick, besides being used for communication, is often employed by other octopus species for camouflage against a static background. But no good example of its being used to mimic another animal has been found before.

The mimic octopus makes up for that. As Dr Norman and his colleagues report in the *Proceedings of the Royal Society*, they are certain their discovery can mimic three other species—sea snakes, banded soles and lion fish. It may also copy sea anemones and jelly fish, though this has not been seen often enough for the team to be sure it was not just coincidental. What all five of these models have in common is that they are venomous (sea snakes bite; soles and lion fish have poisoned spines; anemones and jelly fish sting).

Static images give some inkling of how this is done, but the mimicry is also behavioural (the Royal Society website has videos). And it is appropriate to the circumstances, too. For example, when attacked by damselfish, an octopus reacts by imitating a sea snake, a damselfish predator.

All this allows the mimic octopus to be bolder than its cousins. Those cousins are frequently nocturnal. The mimic forages in daylight under the noses of fish which, if they knew what they were really looking at, would make a tasty snack of it.

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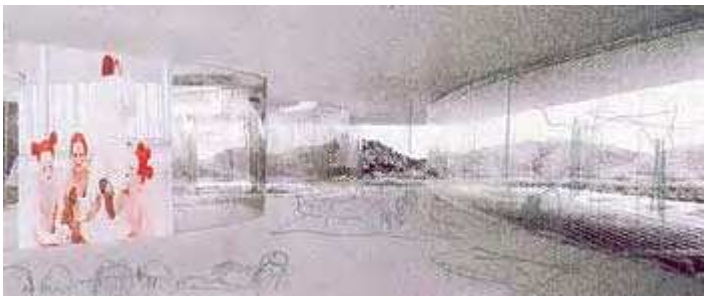
About sponsorship

Showing video art

The glasshouse effect

Aug 30th 2001 | NAPA VALLEY, CALIFORNIA
From The Economist print edition



In the wine country north of San Francisco, two world-famous architects are designing a totally new kind of house for a new kind of art

IMAGINE a glass double helix perched on a ridge above vineyards. Then imagine living in it. From above, it will look like a translucent space ship. From the ground, it will be invisible, hidden behind a vale of trees. Inside, film images, not paintings, will float on curved walls. From within and without, views will stretch to the mountains and the wine country. No straight lines, no curtains, no compromise.

This is the visionary idea for living that Jacques Herzog and Pierre de Meuron put to Dick and Pam Kramlich, an art-collecting couple from San Francisco, after a dinner together in Napa. The Basle-based design team, who created London's Tate Modern and who won the 2001 Pritzker prize for architecture, were in the neighbourhood for their work on the new Dominus Winery. The Kramlichs told them they wanted a house where they could display the film- and video-based art they had been collecting since the late 1980s. On seeing the Herzog-de Meuron plan, they said yes almost on the spot. The foundation is in, and, if all goes to plan, the path-breaking house will be up by 2003.

As you might expect for a treasury of the screen image, the visual idea running through the entire design is careful looking. Rather than tower above it, as do so many new Napa mansions, the Kramlich site nestles into the landscape. The views of Mount St Helena to the north and the Robert Mondavi vineyards to the south are not panoramic but focused.

Pursuing this line of thought, Mr Herzog calls the house “an optical instrument” for viewing a “private and unprivate” collection. It is to be a home to the Kramlichs and a virtual museum, in two senses: the couple intend to show their screen art to the public by appointment. Displaying it, to the Kramlichs, is “a mission”.

A vast basement is being set aside to provide museum-grade gallery space where a fifth of the collection can be shown at a time. An archive and study centre will also be available to scholars. The curator is to be Christopher Eamon of New York's Whitney Museum, who with an art consultant, Thea Westreich, helped build the Kramlich collection.

To serve the house's dual function, the designers have used what they call “material and immaterial architecture”. The gallery basement is a black-box space filled with movable walls, where the architecture is meant to be invisible. “Strong media pieces engage all the senses,” explains Mr Kramlich on a site tour. For sure, experiencing badly installed video art can be all too like involuntary detainment in a hospital ward or an airport lounge, as sound and image from different sources bleed chaotically into one another. So pains have been taken to provide for “interstitial spaces” or airlocks between works.

The public will enter the gallery through a vaulted, trapezoidal lobby, cut into the hillside, to be greeted by an enormous light box showing Jeff Wall's “Untangling”, a mesmerising image of a man in overalls

amid tangled ropes and machines in a boat-shed. The Kramlichs' entrance is through a garage the size of an arthouse cinema, designed to screen Gary Hill's “Viewer” on the far wall and to lead, by way of a glass staircase, to the glass living space above.

In the design, there are no corridors as such, and no separate service spaces: nothing in other words to harden an organic whole and break up its curving films of glass. At the heart of the house is an eye-shaped swimming pool with a retractable roof. Films will project across the water through the glass wall of the kitchen. Every surface in the house—glass, water, the handcrafted textiles that replace curtains, even parts of the garden—could potentially become a screen for art.

If it all sounds too much, Mrs Kramlich points out that living with media art is really no different from living with fixed-image art. (The couple have works by Andy Warhol and Joseph Beuys in their mock-Tudor San Francisco home.) The difference, she adds with an eye to California's electricity troubles, is that you have an on-off switch—and when the images vanish, the house is an artwork of its own.

The Kramlichs are known in the art world for betting on the newest thing. When they began collecting media art, no one else was. The couple bought their first piece, “The Way Things Go” by two Swiss artists, Peter Fischli and David Weiss, at Documenta VIII in 1987, and played it on their VCR. At the time, no one knew how long the technology would last, how to conserve the medium, how to live with it, or what it was worth, financially or aesthetically. Even now these questions are hotly debated. Mrs Kramlich sees their collection as a “life-long learning experience”, and she and her husband consult with different experts in the field. Together with the Tate in London and the Museum of Modern Art in San Francisco, they have established the New Art Trust, which will pay for acquisitions and sponsor critical research in the field of media art.

There is plenty to reflect on. As Mr Kramlich is a venture capitalist, whose firm, NEA, built a fortune investing in new technologies, the link with the latest art techniques might seem a literal and obvious one. But little, if any, of the Kramlich collection is strictly about technology itself. Unlike a painting or a still photograph, the originality of moving-image art is to unroll in time. Indeed, David Ross, an early art-world advocate of media work, wrote in “Seeing Time”, the catalogue for a recent touring exhibition of the Kramlich collection, that film-based and video art marks “the aesthetic transformation of our era”, providing artists with a new means of representing temporal experience.

This is exciting, if tricky, as that slippery phrase “temporal experience” suggests. Nor does media art itself stand still. Last June, at a conference at Tate Modern sponsored by the Kramlichs on the impact of digital technology on art, Laura Mulvey, who is professor of film and media at Birkbeck College, London, spoke about new artistic possibilities in the projection of film fragments or in the showing of whole films in new ways. She cited the four-minute gallery films of Mark Lewis, for example, and Douglas Gordon's “24-hour *Psycho*”, in which Alfred Hitchcock's famous film is drawn out in slow motion beyond what people could possibly watch. “Artists are doing something sculptural and physical with time and film,” Ms Mulvey observed. Yet she noted also that how to catch the passage of time in a still image is an old problem, one that Chardin was exploring over 200 years ago when he painted a boy making a house of cards.

To the Kramlichs, media art not only raises puzzles about time. Its imaginative possibilities offer us a chance, they believe, to slow down and reflect on the role images play in our lives and what new technologies are for. In a museum-house with glass walls, the Kramlichs and their architects hope to have found apt expression for this remarkable vision.

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About sponsorship

The Spanish civil war

Filling in the blanks

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New books on a conflict that divided Europe and defined a generation

La Justicia de Queipo.
By Francisco Espinosa Maestre.
Centro Andaluz del Libro; 383 pages; 4253 pesetas

Soldados de Salamina.
By Javier Cercas.
Tusquets; 209 pages; 2000 pesetas

Maquis: Historia de la guerrilla antifranquista.
By Secundino Serrano.
Temas de Hoy; 430 pages; 3500 pesetas

Spain Betrayed: The Soviet Union in the Spanish Civil War.
Edited by Ronald Radosh, Mary R. Habeck and Grigory Sevostianov.
Yale; 537 pages; $35 and £27.50

El Imperio que nunca existio.
By Gustau Nerin and Alfred Bosch.
Plaza y Janes; 336 pages; 2995 pesetas

A WAR of principle or a dress rehearsal by the totalitarian powers? A struggle between democracy and fascism, or an avoidable and ghastly mess? No civil war in the 20th century, not even ex-Yugoslavia's, divided Europe in quite the same way as Spain's. At its outbreak in 1936, defending the Spanish republic defined choices for a generation; and when it ended three years later in victory for General Franco's *Nacionales*, Spain was politically frozen for almost 40 years. In the dictator's lifetime, the war was virtually untouchable as a public topic in Spain. And when he died in 1975, most Spaniards preferred entrenching democracy to settling old scores or exhuming the past.

Writing the war's history without heroic or exaggerated images of some kind has never been fully achieved, and may not be possible. Sympathetic democrats have stressed the liberal ideals of the republic, and the German planes that bombed the Basque town of Guernica on market-day. Communists have pictured republican Spain as alone against fascism, with only the Soviet Union to help. Right-wing historians who looked on Franco as the lesser evil have played up the chaos and infighting on the republican side.

Not for the first time, new books by Spanish and non-Spanish authors seek to break with old or received ideas about the war, or place it in a broader context. In this they have been helped by new documents, even though tons of evidence were destroyed, through neglect or deliberate attempts to suppress the past.

An old Francoist myth that lived on in some places is the one-sidedness of the violence. Yet hideous persecutions and massacres accompanied the national troops' advance through Spain. In “La Justicia de Queipo” (Queipo's justice), Francisco Espinosa Maestre focuses on the region of Seville, where Gonzalo Queipo de Llano, a notorious Francoist general, broadcast invitations to rape and murder of a kind familiar from ex-Yugoslavia and Rwanda.

Two other books, one a bestselling novel, the other a history, bring out the melancholy fact that, whoever they wanted to win, many Spaniards accepted the final result if only because it meant an end,

as they believed, to the hardship and suffering.

In Javier Cercas's bestselling novel, “Soldados de Salamina” (Soldiers of Salamina), he describes an episode where Franco's troops were greeted with sheer relief by war-weary supporters of the republic. The novel's main thread is equally conciliatory: the true story of Rafael Sanchez Mazas, a falangist whom republican peasants saved from execution.

In “Maquis”, a history of the guerrilleros who went on fighting after 1939, Secundino Serrano describes a failed attempt to free a mountain valley when local people refused to co-operate. Francoist officialdom sought to expunge evidence of resistance after 1939. Yet knots of men, totalling perhaps 5,000-6,000, bravely fought on into the 1950s. Those caught were shot, and their bodies displayed in village squares as warning. Democratic Spain has taken little if any interest in them. As Mr Serrano reminds us, many were communists who got no help from their party. In 1939, orders were given from Moscow to abandon the struggle. Stalin and his envoys could see that the republic was losing the war, a defeat to which communist blunders and machinations had contributed. Naturally, Stalin's men fingered everyone but themselves, including Trotskyists and “fifth-columnists” who they blamed for infiltrating the republic—even though, by the end, Stalinists controlled much of the army and government.

Nobody who saw communist behaviour in Barcelona in May 1937 or who read George Orwell's famous account of those events in “Homage to Catalonia” can have continued to view Stalinism in Spain as a benign presence. But were they even so a bulwark against worse chaos? Ronald Radosh and colleagues have confirmed how hard this line is to defend, using Comintern records from newly (though, alas, selectively) opened Moscow archives.

“Spain Betrayed” presents evidence to show how Spanish gold drained out to Moscow for over-priced Soviet arms, how the international brigades were quickly brought under communist control, and how the 1937 uprising in Barcelona that led to street-fighting between communists and the far left was planned in Moscow, to bring Catalonia under communist control.

Apologists for Franco have often praised him for keeping Spain out of the second world war. A common and persuasive line, upheld by some independent historians, is that to spare his country further hardship and preserve its independence he refused Hitler's invitation to join the war. This view, at best a half truth, is captured in Hitler's famous jibe, after meeting Franco at Hendaye in October 1940, that he would rather have two teeth pulled than endure another meeting with the Spanish leader.

The full truth, according to Gustau Nerin and Alfred Bosch, was different. “El Imperio que nunca existio” (The empire that never existed) argues that Franco went to the 1940 meeting prepared to enter the war, but came out humiliated because he did not get what he wanted: a large slice of North and Equatorial Africa, as well as Gibraltar. In June, Franco had seized international Tangiers, hoping to move on into French-controlled Morocco and rebuild Spain's empire at its defeated neighbour's expense. Hitler had other plans for Africa. After the allied landing in North Africa, Franco embarked on a discreet rapprochement with the Americans. In August 1945, he pulled out of Tangiers and set about tailoring his image.

All of these books are interesting in themselves, and though none of them breaks completely new ground, they add significant detail to our understanding of this terrible European war.

NB: An exhibition of photographs from the Spanish civil war is at the Hôtel de Sully in Paris until September 23rd, and then at the Museu Nacional d'Art de Catalunya in Barcelona (October 10th-January 13th 2002). London's Imperial War Museum (Lambeth, SE1) is also putting on a show about the war (October 20th-April 28th 2002)

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About sponsorship

Algeria then and now

Was de Gaulle pushed?

Aug 30th 2001
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Get article background

Algeria, 1830-2000: A Short History.
By Benjamin Stora. (Translated by Jane Marie Todd).
Cornell University Press; 304 pages; $35. Plymbridge; £23.50

France, The United States, and the Algerian War.
By Irwin M. Wall.
University of California Press; 352 pages; $39.95 and £26.95

EVEN today, thanks to recent confessions by its participants, the savagery of Algeria's eight-year war of independence from France is both shocking and dismaying. The French military herded Algerian civilians into detention camps and security zones—and then let rip with abandon (and napalm) on those outside the zones.

Both sides routinely used terror and torture. By the time the Evian peace accords were signed in 1962, one government after another had collapsed in Paris; part of the French army had mutinied against the state; and out of a population of around 9m Algerians and a million European *pieds-noirs* settlers, several hundred thousand, most of them Algerian, had been killed.

But does such a history explain Algeria's present torment: not just a bloody civil war pitting Islamic fundamentalists against the military-dominated regime but more recently the despairing protests by the country's Berber minority? Benjamin Stora, perhaps France's leading historian of Algeria, refuses to jump to conclusions: modern Algeria, with 60% of the population under the age of 30 and with most people living in the cities, not the countryside, is a far cry from the Algeria which broke free from France two generations ago. Yet, as he points out, there is a “striking mimicry” in the way regime and opposition alike parrot the slogans of the war against France, a mimicry based on a “fabricated memory”: the leaders of the Front de Libération Nationale had created a myth of Algerian nationalism which co-opted Islam and ignored the Berbers. Now the illusions have gone, stripped away by a demographic explosion (the country has more than 30m people) and by the failure of the state to translate petroleum revenues into decent living standards.

While Mr Stora's book (a translation, at times awkward, of three volumes in French) encompasses the whole narrative of modern Algeria, from the first landings of the conquering French, through their ignominious departure and on to Algeria's present agony, Irwin Wall contents himself with just one episode of that narrative: the struggle for independence. But in doing so he fills in some of the gaps in Mr Stora's narrative. Whereas Mr Stora sees Algeria from the perspective of France, Mr Wall takes an outsider's view.

It makes for a useful complement. Whereas Mr Stora's points of reference for the war are usually French and often cultural (he notes the blossoming of French cinema and the opening of the first supermarkets), Mr Wall's are international and geopolitical. His scope is broad: the establishment of NATO; the Suez war; the beginnings of what is now the European Union; the Bay of Pigs fiasco in Cuba; the nervous face-off in the aftermath of the second world war between the West and Russia; the worldwide trend to decolonisation; and the standing demand on America to bail out France from successive balance of payments' crises.

In particular, as Mr Wall notes, he provides an answer to the question left hanging by Mr Stora: namely, given that the French army by the end of the 1950s had more or less won its war in Algeria, why did Algeria nonetheless gain its independence? If Mr Stora is puzzled, Mr Wall is not. The question, he says,

answers itself: the Muslims had been permanently alienated; population growth meant rebel incidents were never likely “to decrease to acceptable or tolerable levels”; French public opinion was sickened; the French intelligentsia was outraged by the practice of torture; and, “just as important”, America could not accept French policy.

Did Charles de Gaulle, summoned back in 1958 to meet France's constitutional crisis and end the Algerian war, realise all this? Conventional wisdom is that he was France's far-sighted saviour, accepting almost from the outset that the loss of Algeria was inevitable. Mr Wall, having trailed through both French and American archives, disagrees. De Gaulle's acceptance of Algerian independence was a belated pragmatism, forced on him by his failure to win over the Americans, first under Eisenhower and then under Kennedy.

Moreover, for all his qualities, what did the general achieve? According to Mr Wall he had three ambitions: to make France part of a “directorate” with America and Britain; to build a European political community based on co-operating nations rather than supranational institutions; and to form a “Eurafrique”, linking France with Algeria and other ex-colonies, as a counterweight to the power of America and Britain. Clearly he failed, and in Mr Wall's view the general's policy of independence for France (witness its nuclear weapons) has subsequently failed too: “Whether in Iraq or Bosnia or Kosovo, the United States has taken the lead; when it abdicates, despite numerous French efforts, there is no European policy to fill the vacuum. France has not been up to the measure of its foreign policy ambitions.” You need not agree with this overall conclusion, with its pessimistic implications for the future, to accept Mr Wall's historical point, that the United States was a critical force in pressing France to accept Algerian independence.

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Sustainable development

Energetic visionaries

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BOOKS IN BRIEF

How to turn the mantra of sustainable development into meaningful action

BACK in 1987, a panel headed by Sweden's Gro Harlem Brundtland defined sustainable development as growth that meets our needs without compromising the ability of future generations to meet theirs. This important new book from the International Energy Agency (IEA), a quasi-governmental agency, argues that that vision "has slowly evolved from a slogan for environmentalists into a guiding principle for public policy."

Toward a Sustainable Energy Future

International Energy Agency; 300 pages; $100

Buy it at Amazon.com

Toward that end, the IEA has produced a how-to manual for pursuing more sustainable energy policies. Smog, acid rain and global warming, for example, are linked at least in part to man's use of fossil fuels. Notably, the work does not gloss over difficulties: it points out that liberalising power markets can make it harder to subsidise renewable energy sources, and that reducing emissions from transport might involve unpopular moves such as raising fuel taxes or ending perks like company cars.

LONG before the term became fashionable, Maurice Strong was a leading advocate of sustainability. The charming Canadian has seamlessly woven together a career in business with green activism and global policymaking. Though the book's writing can be plodding, his remarkable career and personal exuberance save it from dullness.

Where on Earth are We Going?
By Maurice Strong

Texere; 431 pages; $27.95 and £18.99

Buy it at Amazon.com Amazon.co.uk

He helped pull together the Rio Earth Summit in 1992. That gathering saw the largest-ever collection of heads of state, including George Bush senior, launch the effort to tackle climate change. Ironically, its culmination—the Kyoto Protocol—has been rejected by Mr Bush's own son. Even so, Mr Strong hopes that the next big Earth Summit, to be held in Johannesburg in September 2002, can revive the goal of sustainable development, and he offers prescriptions for doing so.

KEITH TUTT also worries about the link between energy and sustainable development. His tone is evangelical: we are "fossil addicts", he writes, caught in a "self-destructive spiral" threatening our survival. You do not, though, need to share Mr Tutt's vision of impending cataclysm to be interested in his profiles of inventors and entrepreneurs searching for clean, bountiful sources of energy.

The Search for Free Energy
By Keith Tutt

Simon & Schuster; 354 pages; £18.99

Buy it at Amazon.co.uk

Mr Tutt writes persuasively that these folk are by no means all quacks. His writing is clear, his reporting thorough and his arguments crisp. A good example of what "The Search for Free Energy" has to offer is his account of cold fusion. This was widely ridiculed as the scam of the century. But Mr Tutt lays out the reasoned case for why some version of this approach could play a role in the future of energy production.

THIS gem provides a contrast with those above, which look to a green future. Tim Flannery casts his gaze back. This is a literate, meticulously researched work on the environmental history of North America. Perhaps this book's greatest

The Eternal Frontier
By Tim Flannery

strength is Mr Flannery's ability to bring ancient, inanimate scenes to life. When he describes the great asteroid that crashed into what is now the Yucatan Peninsula (so ending the era of dinosaurs), he does so in such detail that the reader feels almost afraid.

Atlantic Monthly Press; 432 pages; $27.50.
Heinemann; £20

Buy it at
Amazon.com
Amazon.co.uk

Mr Flannery worries that a continent which has proved so accommodating and adaptable may have met its match in climate change. Controversially, he holds that North America "will feel its effects more violently and well in advance of other continents."

NB: A review of "The Skeptical Environmentalist" by Bjorn Lomborg will appear in these pages later this month

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About sponsorship

Sir Christopher Wren

Monumental

Aug 30th 2001
From The Economist print edition

WHAT couldn't he do? Christopher Wren (1632-1723) is rightly famous as the maker of London's largest and most magnificent cathedral, St Paul's. Yet he came to architecture and town planning almost by chance, in his 30s, from a successful career in astronomy.

His Invention So Fertile: A Life of Christopher Wren
By Adrian Tinniswood

Jonathan Cape; 480 pages; £25. Oxford University Press; $35 (December)

Buy it at
Amazon.com
Amazon.co.uk

As a boy, Wren invented unusual sundials and dabbled in engineering. Admitted to university at the age of 17, he found plenty of outlets for his restless imagination. He worked on (among other things) refraction, optics, motion, a history of the seasons, an explanation of the rings of Saturn, maps of the moon, magnetism, navigation, microscopy, anatomy and the intravenous injection. His experiments on live dogs—described in stomach-turning detail in the opening pages of Adrian Tinniswood's book—opened the way for the first attempts at blood transfusion.

In 1653, this “miracle of youth”, as John Evelyn called him, was elected to a fellowship at All Souls College, Oxford; four years later he was professor of geometry at Gresham College, London. There he started up a scientific discussion group which, in 1662, received a royal charter and became the Royal Society.

Curiously, Wren appears to have been little interested in seeing his scientific projects to completion. Though he longed for success, and worked hard to achieve it, he seems to have enjoyed setting himself problems and solving them, leaving the developments and refinements to others.

Wren's first architectural commission—a new chapel for Pembroke College, Cambridge—came in 1663. Though conservative and necessarily small-scale, this elegant, thoroughly classical building is a fine precursor of his later, grander achievements. London's great fire in 1666 was the making of Wren's architectural career. In 1669 he was appointed surveyor general of the royal buildings, replanning the entire city and supervising the building or rebuilding of 51 churches.

Little is known about Wren's personal life. He married twice and had four children, one of whom died at 17 months; another, Billy, was born retarded. Mr Tinniswood, drawing on the work of scholars such as Sir John Summerson and Kerry Downes, has written a highly readable and engaging biography of a fascinating, enigmatic figure.

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About sponsorship

Film feuds

Everyone says I sue you

Aug 30th 2001
From The Economist print edition

Deconstructing Woody
Woody Allen's American box office

Title	Year	Estimated budget, $m	American box office, $m	Objects of desire
Small Time Crooks	2000	18	17.1	Tracey Ullman, Elaine May
Sweet and Lowdown	1999	na	4.2	Samantha Morton, Uma Thurman
Celebrity	1998	na	5.0	Melanie Griffith, Winona Ryder, Charlize Theron
Deconstructing Harry	1997	20	10.7	Elisabeth Shue, Judy Davis, Demi Moore
Everyone Says I Love You	1996	20	9.7	Julia Roberts, Drew Barrymore, Goldie Hawn
Mighty Aphrodite	1995	na	6.4	Mira Sorvino, Helena Bonham Carter
Bullets over Broadway	1994	20	13.4	Dianne Wiest, Jennifer Tilly
Manhattan Murder Mystery	1993	13.5	11.3	Diane Keaton, Anjelica Huston
Husbands and Wives	1992	20	10.6	Mia Farrow, Judy Davis, Juliette Lewis

Sources: AC Nielsen EDI; *Variety*; *Internet Movie Database*

WOODY ALLEN is one of life's most famous worryworts. With good reason, it seems. He feuded, famously, with Mia Farrow over his affair with the adopted sister of their three children. He battled against the construction of a high-rise building in his beloved Manhattan neighbourhood while at the same time letting builders into his new home; never an easy undertaking. Now, just as his latest film, “The Curse of the Jade Scorpion”, opens in America, it is his business dealings that are the source of renewed heartache.

Virtually none of Mr Allen's films makes money in America. But that didn't seem to matter while his production partner was Jean Doumanian and the films were being secretly bankrolled by her long-time boyfriend, Jacqui Safra, a scion of the billionaire banking family. Yet the friends who have known each other for nearly 40 years are at daggers drawn. Mr Allen is suing Ms Doumanian for withholding financial information from him; she is counter-suing for money that she says he owes her. The quarrel is set to grow even bloodier on its way to court later this year. “The Curse of the Jade Scorpion” has arrived.

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About sponsorship

Cities and writers

Sunny side up

Aug 30th 2001
From The Economist print edition

BLOOMSBURY'S new series of short travel books, the Writer and the City, is shaping up nicely. Peter Carey's “30 Days in Sydney” follows Edmund White's engaging book about Paris, “The Flâneur”, which appeared last year. Like Mr White, Mr Carey writes about an adopted city, not his home town: he grew up in rural Victoria and has lived in New York for the past ten years. But Sydney still calls him. It is a place for which he harbours strong, if mixed, feelings.

30 Days in Sydney: A Wildly Distorted Account
By Peter Carey

Bloomsbury; 256 pages; $16.95 and £9.99

Buy it at
Amazon.com
Amazon.co.uk

Mr Carey touches down at Kingsford Smith airport with an idea of the form he wants his book to take. Tape recorder in hand, he will meet up with some old friends and ask them to talk about one of the four ancient elements: earth, air, fire and water.

His oddball pals oblige with often hilarious accounts of storms at sea, conflagrations on land and other hair-raising misadventures. These deftly link in with threads of narrative and history. Mr Carey's subtitle is “A Wildly Distorted Account”, and, for all its apparent casualness, there's more than a hint here of the novelist's art.

“How can I hope to convey to any reader my idea of Sydney?” he muses.

> I have seen nothing to equal it in the way of landlocked scenery, in the particular relationship between the races, in the easy tolerance of crime and corruption, in the familiar mingling you can witness on the footpath outside Bar Coluzzi any morning, where you may find judges and writers and the euphemistically labelled ‘colourful racing identities'all bunched happily together in the sunshine, somehow feeling themselves to be at the red-hot centre of the town.

This is disingenuous. “30 Days in Sydney” is the next best thing to, well, 30 days in Sydney.

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About sponsorship

Sir Fred Hoyle

Aug 30th 2001
From The Economist print edition

Sir Fred Hoyle, scientist and rebel, died on August 20th, aged 86

Corbis

RACIAL stereotypes are always dangerous, but Fred Hoyle would probably not have objected to the use of the term “gritty” in connection with his own ethnic origins in Yorkshire, in northern England. Despite his fellowship at St John's College, Cambridge, he was never comfortable as part of Britain's intellectual establishment. Yet, in his time, he was probably the country's most famous astronomer, and certainly one of its most famous scientists.

That is all the more remarkable because his best-known idea from his early life has turned out to be wrong, and his best-known idea from his later life is regarded by most researchers in the field as, frankly, batty. Between these two mis-steps, however, Sir Fred worked out the not insignificant detail of why chemistry is diverse enough to support the complex material phenomenon known as “life”.

His earlier mis-step was cosmological, and it was as a cosmologist that he became famous. In 1925, Georges Le Maitre, a Belgian monk, proposed that the universe had once been tiny, and had exploded in a cosmic fireball of which the galaxies are the remnants. This idea became popular, but Fred Hoyle hated it. In 1948, he counter-attacked. His assault was two-pronged. First, he suggested an alternative: that the universe is infinitely old, and that new matter appears spontaneously to fill the gaps as it expands. Second, he proposed a ridiculous name for his opponents' idea, in the hope of humiliating them. He called it the “Big Bang”.

The attack failed on both counts. Le Maitre's disciples loved the name, and adopted it. Meanwhile, evidence in their favour accumulated to the point where it became overwhelming. That was no disgrace. Sir Fred's “Steady State” theory fitted the evidence available at the time it was proposed, and forced the Big Bangers to defend their position. Testing such competing hypotheses is how science is supposed to proceed. And some of his other hypotheses have stood up well to scrutiny: in particular those concerning the creation of heavy elements.

The Nobel controversy

Neither the Big Bang, nor the Steady State versions of cosmology account for any but the lightest elements—hydrogen and helium. Fred Hoyle showed how the rest of the periodic table could be built up. The problem of the heavy elements is actually two problems. Sir Fred solved them both. Stars shine by nuclear fusion—the merging of light atomic nuclei to release energy. The reaction between hydrogen atoms to make helium has the biggest yield, but subsequent mergers all the way up to iron (number 26 on the periodic table) will release some energy. For heavier nuclei, though, the reverse is true. These release energy when they are broken down. For really heavy elements, such as uranium, such fission happens spontaneously.

In theory, making elements up to iron should not be hard. However, until Fred Hoyle applied his mind to the question it looked as though many of the intermediate steps might be too unstable to account for the quantities of those elements that are observed. In 1954, though, he showed how these intermediate nuclei are stabilised by internal resonances that enable them to last long enough for the next fusion step to take place. In 1957, he and three colleagues wrote a paper showing how elements heavier than iron are produced. They are made in exploding stars called supernovae, in which the energies are so high that nuclei get squashed together into otherwise unstable configurations.

This was Nobel-prizewinning stuff, and William Fowler, one of the paper's authors, duly got the call from Stockholm. That was widely regarded as unfair, for many of the key insights were Fred Hoyle's. Whether his knighthood in 1972 made up for the disappointment is doubtful. For whatever reason, though, he began to turn away from cosmology.

He had long been interested in the idea of life in space, but that interest was initially expressed only in his science-fiction. “The Black Cloud”, published in 1957, is perhaps the best of these stories. It describes a life form that inhabits a small nebula known as a Bok globule, which visits the solar system to refuel from the sun.

An interesting idea. But one that got out of hand when he met Chandra Wickramasinghe (then a student, now a professor at the University of Wales). The two of them decided to revive the theory of “panspermia”—that life is ubiquitous, and spreads from planet to planet as a sort of infection. This is an old idea. It might even be true. However, Sir Fred and Dr Wickramasinghe took it to ridiculous lengths, proposing not only the arrival of organisms from outer space, but that those organisms (such as influenza viruses) are somehow already adapted for life in the hurly-burly of the terrestrial ecosystem.

It is not unknown for good scientists to go off the rails at the end of their careers, and Fred Hoyle did so in spectacular style. The theory got sillier and sillier. He once suggested that bees are ideally adapted for interplanetary life. Being a Yorkshireman, he was also loth to admit error. He never reconciled himself to the Big Bang, nor to the idea that influenza epidemics start in pigs and poultry, not in outer space. But he did explain the elements. That is hardly a bad epitaph.

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Overview

Aug 30th 2001
From The Economist print edition

America narrowly avoided an output fall in the second quarter. According to revised figures, GDP grew at an annual rate of 0.2% in the second quarter, the slowest in more than eight years. This was lower than the preliminary estimate of 0.7%, but still better than the markets had expected.

Things do not look good in the third quarter, however. The Conference Board's index of consumer confidence fell unexpectedly, led by the most pessimistic assessment of the situation for over four years. Much of the gloom reflected deteriorating labour-market conditions. Only 33% of respondents felt that jobs were plentiful, down from over 50% a year ago. Durable-goods orders fell by 0.6% in July, leaving them 11.2% lower than a year ago. There are no signs of recovery yet in computers and electronics orders, which fell by 4.4% in July.

In the **euro area**, there was more evidence of improving confidence. The July Belgian BNB index showed a balance of 10.8% of respondents who felt that business conditions were bad compared with those who thought business was good, a slight improvement over June's 11.0% reading. Dutch business confidence improved as well, its first rise in ten months. Taken together with last week's surprise improvement in Germany's IFO index, these surveys offer hope that Europe may be bottoming out.

According to preliminary estimates, **Germany's** consumer-price inflation was unchanged at 2.6% in the year to August; inflation fell slightly in **Italy** to 2.8%. But broad-money growth jumped unexpectedly in the euro area to 6.4% in the year to July, from 6.1% in June. Despite this, the European Central Bank cut its key interest rate by a quarter-point, to 4.25%.

Japan's unemployment rate reached a record high of 5.0% in July, automatically activating emergency federal hiring subsidies. Meanwhile, plummeting exports brought the seasonally adjusted trade surplus to ¥335 billion in July, down from ¥649 billion in the previous month, and the lowest level since 1983. And Japanese industrial production fell by 8.5% in the year to July. The Nikkei tumbled to a 17-year low as investors dumped bank stocks on worries over bad loans.

The Bank of **Canada** cut its bank rate by a quarter-point to 4.25%, citing weakening domestic demand.

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Output, demand and jobs

Aug 30th 2001
From The Economist print edition

% change at annual rate

	GDP		The Economist poll GDP forecasts		Industrial production	Retail sales (volume)	Unemployment % rate	
	1 qtr	1 year	2001	2002	1 year	1 year	latest	year ago
Australia	+ 4.3	+ 2.1 Q1	+ 2.6	+ 4.0	– 1.4 Q1*	+ 0.7 Q2	6.9 Jul	6.1
Austria	+ 1.6	+ 2.2 Q1	+ 1.8	+ 2.3	+ 8.0 Jun	– 1.5 Apr	3.8 Jul	3.6
Belgium	– 2.4	+ 1.7 Q2	+ 2.1	+ 2.4	– 0.5 Jun*	– 3.4 May	11.1 Jul*	11.2
Britain	+ 1.4	+ 2.1 Q2	+ 2.2	+ 2.7	– 2.2 Jun	+ 6.0 Jul	5.0 Jun‡	5.5
Canada	+ 2.5	+ 2.6 Q1†	+ 2.2	+ 3.1	– 0.7 May	+ 3.6 May	7.0 Jul	6.8
Denmark	– 4.6	+ 1.0 Q1	+ 1.4	+ 2.1	+ 4.4 Jun	+ 3.0 Jun	5.2 Jun	5.4
France	+ 2.0	+ 2.7 Q1	+ 2.2	+ 2.4	+ 2.3 Jun	+ 2.3 Jun	8.8 Jun	9.5
Germany	nil	+ 0.6 Q2	+ 1.2	+ 2.0	+ 0.9 Jun	+ 0.5 Jun	9.3 Jul	9.5
Italy	– 0.5	+ 2.0 Q2	+ 2.0	+ 2.3	– 3.1 Jun	– 1.2 May	9.5 Apr	10.7
Japan	+ 0.5	+ 0.2 Q1	– 0.5	+ 0.7	– 8.5 Jul	– 2.4 Jun	5.0 Jul	4.7
Netherlands	+ 1.6	+ 1.5 Q2	+ 2.0	+ 2.8	+ 0.7 Jun	+ 1.5 Mar	2.0 Jul§	2.6
Spain	+ 4.1	+ 3.3 Q1	+ 2.7	+ 2.9	– 2.6 Jun	na	12.8 Jul	14.0
Sweden	+ 1.3	+ 1.4 Q2	+ 2.2	+ 2.7	– 1.0 May	+ 2.1 Jun	4.2 Jul*	5.2
Switzerland	+ 7.4	+ 2.5 Q1	+ 1.7	+ 2.0	+ 5.1 Q1*	+ 8.4 Jun	1.7 Jul*	1.8
United States	+ 0.2	+ 1.2 Q2	+ 1.6	+ 2.7	– 3.2 Jul	+ 2.5 Apr	4.5 Jul	4.0
Euro area	+ 2.0	+ 2.5 Q1	+ 1.9	+ 2.3	+ 1.4 Jun	+ 0.5 May	8.3 Jun	8.9
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*							
Finland	– 0.4	+ 3.4 Q1	na	na	– 5.4 Jul	+ 2.2 May	7.6 Jul*	7.8
Greece	na	+ 2.52000	na	na	– 0.8 Mar*	+ 5.1 Mar	na	na
Iceland	na	+ 3.62000	na	na	+ 2.5 2000	na	1.3 Jun	1.4
Ireland	na	+12.1 Q4	na	na	+13.9 Jun*	+ 0.7 May	3.6 Jul	4.0
Luxembourg	na	+ 8.52000	na	na	+ 1.4 May*†	+ 9.1 Jun	2.4 Jun	2.7
New Zealand	+ 0.9	+ 0.4 Q1	na	na	+ 0.9 Q1*	+ 7.2 Q2	5.2 Q2	6.1
Norway	+ 0.9	+ 0.3 Q1	na	na	– 0.1 Jun*	– 1.1 Jun	3.6 Q2	3.3
Portugal	– 0.3	+ 2.2 Q1	na	na	+ 5.1 Jun*	+ 2.2 May	4.2 Q1	4.4

*Not seasonally adjusted. †New series. ‡Mar-May; claimant count rate 3.2% in Jun. §May-Jul.

Text refers only to the first 16 countries listed

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Prices and wages

Aug 30th 2001
From The Economist print edition

% change at annual rate

	Consumer prices*			The Economist poll consumer prices forecast		Producer prices*			Wages/earnings		
	1 year		year ago	2001	2002	1 year		year ago	1 year		year ago
Australia	+ 6.0	Q2	+ 3.2	+ 3.9	+ 2.4	+ 5.6	Q2	+ 7.4	+ 3.7	Q2	+ 3.9
Austria	+ 2.7	Jul	+ 2.8	+ 2.5	+ 1.8	+ 1.9	Jul	+ 4.6	+ 2.8	Jul	+ 2.0
Belgium	+ 2.7	Jul	+ 2.8	+ 2.6	+ 2.0	+ 4.0	Jun	+ 8.7	+ 2.6	Q2	+ 2.2
Britain	+ 1.6	Jul	+ 3.3	+ 2.1	+ 2.4	+ 0.1	Jul	+ 2.7	+ 4.8	Jun	+ 4.1
Canada	+ 2.6	Jul	+ 3.0	+ 2.8	+ 2.1	+ 0.9	Jul	+ 4.2	+ 1.7	Jun	+ 1.0
Denmark	+ 2.4	Jul	+ 3.1	+ 2.4	+ 2.1	+ 2.7	Jul	+ 5.8	+ 3.8	Q1	+ 3.6
France	+ 2.1	Jul	+ 1.7	+ 1.8	+ 1.5	+ 2.3	Jun	+ 6.0	+ 4.3	Q1	+ 5.2
Germany	+ 2.6	Aug	+ 1.8	+ 2.7	+ 1.7	+ 2.2	Jul	+ 5.5	+ 1.8	Jun*	+ 2.1
Italy	+ 2.8	Aug	+ 2.6	+ 2.8	+ 2.0	+ 2.3	Jun	+ 6.9	+ 2.7	Jun*	+ 1.8
Japan	− 0.5	Jun	− 0.7	− 0.4	− 0.4	+ 0.8	Jul	− 0.4	+ 0.9	Jun	+ 2.8
Netherlands	+ 4.6	Jul	+ 2.8	+ 4.6	+ 2.7	+ 4.3	Jun	+ 8.8	+ 4.4	Jul	+ 3.2
Spain	+ 3.9	Jul	+ 3.6	+ 3.7	+ 2.8	+ 2.4	Jun	+ 5.8	+ 2.2	Q4	+ 2.4
Sweden	+ 2.9	Jul	+ 1.2	+ 2.3	+ 1.8	+ 2.1	Jul	+ 3.7	+ 2.7	May*	+ 1.9
Switzerland	+ 1.4	Jul	+ 1.9	+ 1.3	+ 1.3	+ 0.2	Jul	+ 2.7	+ 1.3	2000	+ 0.3
United States	+ 2.7	Jul	+ 3.7	+ 3.2	+ 2.2	+ 1.5	Jul	+ 4.3	+ 4.4	Jul	+ 3.6
Euro area	+ 2.8	Jul	+ 2.3	+ 2.8	+ 1.9	+ 3.3	Jun	+ 5.6	+ 2.6	Q1	+ 2.4
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 2.5	Jul	+ 3.7	na	na	+ 0.7	Jul	+ 8.0	+ 4.8	Q2*	+ 4.6
Greece	+ 3.8	Jul	+ 2.7	na	na	+ 5.1	Apr	+ 7.0	na		na
Iceland	+ 7.9	Aug	+ 4.7	na	na	+ 6.9	Aug	+ 3.5	+ 8.1	Jul	+ 7.9
Ireland	+ 4.8	Jul	+ 6.2	na	na	+ 2.6	Jul	+ 5.6	+ 6.4	Q4*	+ 7.3
Luxembourg	+ 3.0	Jul	+ 3.4	na	na	nil	Jun	+ 5.5	+ 2.4	May*	+ 8.4
New Zealand	+ 3.2	Q2	+ 2.0	na	na	+ 7.8	Q1	+ 4.9	+ 1.8	Q2	+ 1.7
Norway	+ 2.7	Jul	+ 3.3	na	na	− 3.1	Jul	+ 6.4	+ 4.4	Q1*	+ 4.1
Portugal	+ 4.3	Jul	+ 3.2	na	na	+ 4.2	Jun	+16.2	+ 2.4	Apr*	na

*Not seasonally adjusted.

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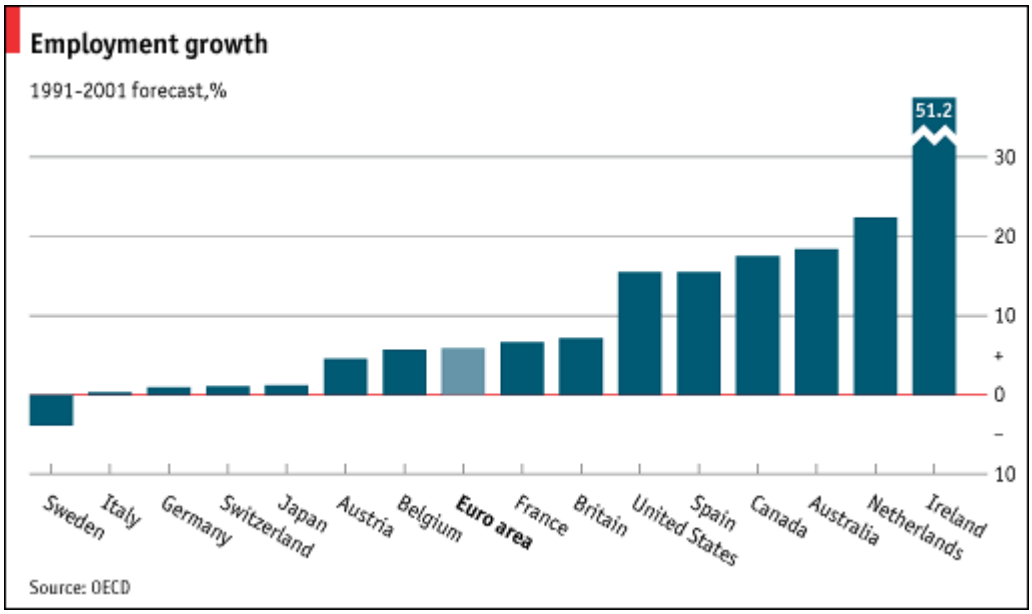
Employment growth

Aug 30th 2001
From The Economist print edition

Between 1991 and 2001, estimates the OECD, employment in the roaring Irish economy will have increased by more than half. It is no surprise that Ireland, for decades an exporter of people, has turned into a land of net immigration. The Dutch, Australians, Canadians and Spanish have also all created proportionately more jobs than even the booming American economy over the past ten years. Sweden has lost jobs; in Italy, Germany and Japan employment growth has been broadly stagnant.



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Money and interest rates

Aug 30th 2001
From The Economist print edition

	Money supply* % change on year ago			Interest rates % p.a. (Aug 29th 2001)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+15.8	+ 7.0	Jun	4.82	6.57	4.74	5.49	6.29	6.94
Britain	+ 7.1	+ 7.6	Jul	4.91	6.19	4.93	4.81	5.32	6.04
Canada	+ 6.9	+ 4.8	Jul	3.82	5.68	4.23	5.36	5.77	7.02
Denmark	+ 3.4	– 5.5	Jun	4.67	5.83	4.45	5.02	5.60	7.07
Japan	+ 8.7	+ 3.3	Jul	0.03	0.32	0.04	1.35	1.87	1.47
Sweden	+ 6.5	+ 2.2	Jul	4.27	3.89	4.47	5.07	5.26	5.27
Switzerland	+ 0.3	+ 3.0	Jul	3.21	3.48	3.42	3.28	3.76	4.05
United States	+ 3.0	+11.5	Jul	3.38	6.48	3.63	4.85	5.95	6.80
Euro area†	+ 3.3	+ 6.4	Jul	4.27	4.89	4.00	4.74	5.22	5.33

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. Benchmarks: US 30-year 5.40%, Japan No.234 1.39%. Central bank rates: US fed funds 3.50%, ECB refinancing 4.50%, BOJ overnight call 0.01%, BOE repo 5.00%.
Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, OM Fixed Income Exchange, Warburg Dillon Read, DRI-WEFA, Westpac, Thomson Financial Datastream. Rates cannot be construed as banks' offers.

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Commodity price index

Aug 30th 2001
From The Economist print edition

1995=100

	Aug 21st	Aug 28th*	% change on one month	% change on one year
Dollar index				
All items	68.3	68.4	– 1.3	– 5.3
Food	69.5	68.8	– 2.6	– 2.0
Industrials				
All	66.8	67.8	+ 0.5	– 9.6
Nfa†	66.8	67.2	– 0.7	– 0.0
Metals	66.8	68.3	+ 1.5	–16.2
Sterling index				
All items	74.4	74.5	– 2.9	– 4.6
Euro index				
All items	98.5	98.9	– 5.0	– 6.7
Yen index				
All items	87.1	87.8	– 4.6	+ 7.7
Gold				
$ per oz	276.55	272.20	+ 2.3	– 0.4
West Texas Intermediate				
$ per barrel	28.20	27.22	+ 1.8	–16.8

* Provisional. † Non-food agriculturals.

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Stockmarkets

Aug 30th 2001
From The Economist print edition

Market indices

	Aug 29th	2001 high	2001 low	% change on one week	% change on record high	% change on Dec 31st 2000 in local currency	% change on Dec 31st 2000 in $ terms
Australia (All Ordinaries)	3,288.4	3,425.2	3,094.3	+ 1.0	- 4.0	+ 4.2	- 0.7
Austria (ATX)	1,208.8	1,245.8	1,052.2	+ 0.3	-30.4	+12.6	+ 9.2
Belgium (Bel 20)	2,900.0	3,030.4	2,591.6	+ 1.8	-21.2	- 4.1	- 7.0
Britain (FTSE 100)	5,417.6	6,334.5	5,275.7	+ 0.2	-21.8	-12.9	-15.4
Canada (Toronto Composite)	7,494.3	9,348.4	7,415.5	- 0.6	-34.2	-16.1	-18.4
Denmark (KBX)	240.3	294.3	234.7	- 2.4	-20.4	- 9.2	-11.7
France (SBF 250)	3,121.4	3,820.2	3,084.7	+ 0.5	-28.9	-17.2	-19.7
(CAC 40)	4,834.9	5,998.5	4,773.2	+ 0.5	-30.2	-18.4	-20.9
Germany (Xetra DAX)	5,305.0	6,795.1	5,207.8	+ 1.6	-34.2	-17.5	-20.0
Italy (BCI)	1,556.0	1,948.4	1,540.9	+ 0.0	-28.7	-18.8	-21.3
Japan (Nikkei 225)	10,979.8	14,529.4	10,979.8	- 3.7	-71.8	-20.4	-23.9
(Topix)	1,126.9	1,441.0	1,126.9	- 3.3	-60.9	-12.2	-16.1
Netherlands (AEX)	535.5	642.3	518.3	+ 1.7	-23.7	-16.0	-18.6
Spain (Madrid SE)	819.0	963.9	798.6	+ 0.9	-28.6	- 7.0	- 9.8
Sweden (Affarsvarlden Gen)	221.7	293.1	214.8	+ 0.7	-44.6	-20.2	-27.3
Switzerland (Swiss Market)	6,580.6	8,135.4	6,574.0	- 1.2	-21.8	-19.1	-21.4
United States (DJIA)	10,090.9	11,337.9	9,389.5	- 1.8	-13.9	- 6.5	- 6.5
(S&P 500)	1,148.6	1,373.7	1,103.3	- 1.4	-24.8	-13.0	-13.0
(Nasdaq Comp)	1,843.2	2,859.2	1,638.8	- 0.9	-63.5	-25.4	-25.4
Europe (FTSE Eurotop 300)*	1,283.5	1,545.5	1,262.6	+ 0.7	-24.7	-16.3	-18.9
Euro area (FTSE Ebloc 100)*	1,136.4	1,404.1	1,117.0	+ 1.0	-26.7	-18.4	-20.9
World (MSCI)†	1,033.2	1,249.2	1,014.6	- 1.1	-28.7	na	-15.4
World bond market (Salomon)‡	450.5	451.0	420.6	- 0.1	- 2.0	na	+ 1.5

*In euro terms. †Morgan Stanley Capital International index includes individual markets listed above plus eight others, in dollar terms.
‡Salomon Smith Barney World Government Bond Index, total return, in dollar terms.

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Trade, exchange rates and budgets

Aug 30th 2001
From The Economist print edition

	Trade balance*, $bn latest 12 months		Current account $bn latest 12 mths		The Economist poll % of GDP, forecast 2001	2002	Exchange rate trade-weighted† Aug 29th	year ago	Currency units per $ Aug 29th	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2001‡
Australia	+ 0.7	Jul	− 9.9	Q2	− 2.9	− 3.1	72.8	76.2	1.89	1.75	2.74	1.72	1.58	0.1
Austria	− 5.4	May	− 4.3	Jun	− 2.3	− 2.2	100.4	99.5	15.1	15.4	22.0	13.8	12.7	-0.6
Belgium	+ 10.6	Jun	+ 11.2	Mar	+ 4.3	+ 4.5	99.2	98.1	44.3	45.2	64.3	40.3	37.1	0.7
Britain	− 44.9	Jun	− 19.2	Q1	− 1.8	− 2.1	105.3	105.7	0.69	0.69	–	0.63	0.58	1.2
Canada	+ 47.4	Jun	+ 22.2	Q1	+ 3.1	+ 2.4	77.6	80.6	1.54	1.48	2.24	1.41	1.29	2.6
Denmark	+ 6.9	Jun	+ 4.5	Jun	+ 1.4	+ 1.4	102.7	100.1	8.18	8.35	11.9	7.44	6.84	2.9
France	nil	Jun	+ 14.3	Jun	+ 1.6	+ 1.6	101.9	100.7	7.21	7.34	10.5	6.56	6.03	-0.5
Germany	+ 57.2	Jun	− 21.8	Jun	− 1.0	− 0.8	98.9	97.2	2.15	2.19	3.12	1.96	1.80	-1.7
Italy	+ 3.3	May	− 4.9	May	− 0.3	− 0.2	72.7	71.9	2,127	2,167	3,088	1,936	1,780	-1.3
Japan	+ 90.4	Jun	+ 96.3	Jun	+ 2.2	+ 2.1	140.0	157.6	120	107	174	109	–	-6.3
Netherlands	+ 18.9	Jun	+ 13.7	Q2	+ 3.9	+ 3.9	98.2	96.8	2.42	2.47	3.51	2.20	2.03	1.3
Spain	− 38.2	May	− 15.9	Apr	− 2.8	− 2.3	74.4	73.6	183	186	265	166	153	nil
Sweden	+ 11.8	Jul	+ 5.6	Jun	+ 2.1	+ 2.3	74.3	82.3	10.37	9.42	15.1	9.44	8.67	3.6
Switzerland	+ 0.3	Jul	+ 28.3	Q1	+11.0	+10.8	108.9	105.1	1.67	1.73	2.42	1.52	1.40	na
United States	−453.5	Jun	−449.3	Q1	− 4.1	− 4.0	117.0	112.2	–	–	1.45	0.91	0.84	2.1
Euro area	− 1.2	May	− 28.0	Jun	− 0.2	− 0.1	79.4	77.4	1.10	1.12	1.59	–	0.92	-0.6
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 14.1	Jun	+ 9.3	Jun	na	na	78.7	76.4	6.53	6.66	9.48	5.95	5.47	5.3
Greece	− 7.5	Jan	− 7.7	Jan	na	na	57.5	57.4	374	378	543	341	313	nil
Iceland	− 0.4	Jun	− 0.9	Q1	na	na	na	na	99	80.8	144	90.2	82.9	2.4
Ireland	+ 29.1	Jun	− 1.3	Q1	na	na	87.8	86.2	0.87	0.88	1.26	0.79	0.72	4.5
Luxembourg	− 2.5	May	+ 1.2	Q1	na	na	99.2	98.1	44.3	45.2	64.3	40.3	37.1	3.6
New Zealand	nil	Jul	− 2.3	Q1	na	na	82.7	76.6	2.27	2.34	3.29	2.06	1.90	1.0
Norway	+ 28.0	Jul	+ 25.6	May	na	na	95.6	92.5	8.86	9.04	12.9	8.07	7.41	15.3
Portugal	− 13.7	May	− 9.2	Jun	na	na	89.6	88.6	220	224	320	200	184	-1.2

*Merchandise, Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †1990=100, Bank of England. ‡OECD estimate.

Text refers only to the first 16 countries listed

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Trade-weighted exchange rates

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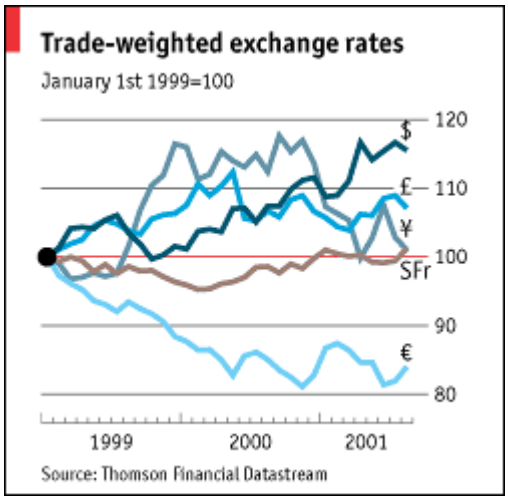
From The Economist print edition

A country's trade-weighted exchange rate is a measure of the price competitiveness of its exports. The euro has gained competitiveness in recent years: it has jogged between 80% and 90% of its January 1999 value for over a year. The dollar and sterling have remained stubbornly high.



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Overview

Aug 30th 2001
From The Economist print edition

Argentina's overnight lending rate fell to 4.75-5.75% on reports that the IMF wanted to swap a larger amount of debt than had originally been expected. Last week, the IMF offered $3 billion to Argentina if it would undertake a voluntary debt exchange as part of an $8 billion emergency package. The overnight lending rate had peaked at 35% on August 21st.

Brazil's overall public sector deficit, which includes debt-service payments, ballooned to 14.34 billion *reais* ($5.8 billion) in July compared with a surplus of 461m *reais* in June. Excluding debt payments, however, the public sector ran a surplus of 2.71 billion *reais*, which was larger than expected. Brazil's stockmarket was tentatively optimistic, rising by 0.8%, but Argentina's fell by 0.9%.

Malaysia's GDP grew by 1.0% in the second quarter after contracting in the first. But since the data were not seasonally adjusted, economists were split over whether it had joined Singapore and Taiwan in recession.

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External-debt-to-export ratio

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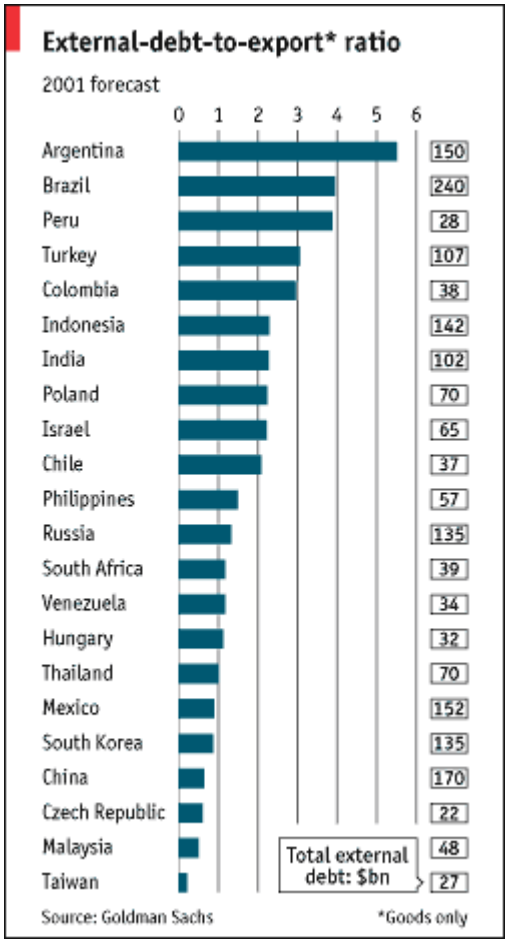
From The Economist print edition

Goldman Sachs forecasts that Latin American countries, led by Argentina, will have the highest external-debt-to-export ratios in 2001, reflecting the weakness of their external accounts and their vulnerability to foreign capital flows. Turkey, too, is at risk. By contrast, the East Asian economies are in a much stronger external position.



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Economy

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From The Economist print edition

	% change on year earlier						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 7.8	Q2	+ 8.1	Jul	+ 1.5	Jul	+19.9	Jul	+20.5	2000	182.0	May
Hong Kong	+ 2.5	Q1	– 0.1	Q1	– 0.9	Jul	–12.1	Jul	+ 8.8	Q1	114.6	Jul
India	+ 5.7	Q3	+ 1.5	Jun	+ 3.4	Jun	– 5.3	Jun	– 2.3	Q1	40.9	Jul
Indonesia	+ 3.5	Q2	+ 4.5	Q4	+13.0	Jul	+24.8	Jun	+ 6.3	Q1	27.9	Jun
Malaysia	+ 0.5	Q2	– 9.9	Jun	+ 1.4	Jul	+15.3	Jun	+ 7.4	Q1	25.6	Jun
Philippines	+ 3.3	Q2	+11.2	Jun	+ 6.8	Jul	+ 5.1	Jun	+ 8.5	Apr	12.5	May
Singapore	– 0.9	Q2	–13.2	Jul	+ 1.3	Jul	+ 4.6	Jul	+22.6	Q2	76.0	May
South Korea	+ 2.7	Q2	– 2.7	Jun	+ 5.0	Jul	+14.0	Jul	+13.3	Jul	94.3	Jun
Taiwan	– 2.4	Q2	–10.4	Jul	+ 0.1	Jul	+12.6	Jul	+14.1	Q2	109.1	Jun
Thailand	+ 1.8	Q1	+ 1.7	Jun	+ 2.2	Jul	+ 3.1	Jun	+ 6.9	Jun	31.0	Jun
Argentina	– 2.1	Q1	+ 0.2	Jul	– 1.0	Jul	+ 2.3	Jun	– 9.0	Q1	21.1	Jun
Brazil	+ 0.8	Q2	– 1.4	Jun	+ 7.8	Jul	– 1.6	Jul	–27.5	Jul	37.3	Jun
Chile	+ 3.4	Q2	+ 0.3	Jul	+ 3.2	Jul	+ 1.5	Jul	– 1.6	Q2	14.3	Jun
Colombia	+ 1.6	Q2	– 2.6	Jun	+ 8.1	Jul	+ 1.3	Jun	– 0.7	Q1	9.5	Jul
Mexico	nil	Q2	– 3.9	Jun	+ 5.9	Jul	– 9.6	Jul	–17.5	Q2	40.8	Jun
Peru	– 2.3	Jun	+ 1.3	May	+ 2.2	Jul	– 0.2	Jun	– 1.4	Q2	8.3	May
Venezuela	+ 2.9	Q2	na		+13.0	Jul	+17.2	Q1‡	+11.3	Q2	10.5	Jun
Egypt	+ 6.5	2000†	+ 9.4	2000†	+ 2.2	May	– 9.9	Q1	– 0.2	Q1	13.0	Apr
Israel	+ 1.4	Q2	– 6.3	May	+ 0.4	Jul	– 7.3	Jul	– 1.1	Q1	23.9	Jul
South Africa	+ 2.5	Q2	+ 3.1	Jun	+ 5.3	Jul	+ 4.1	Jun	+ 0.1	Q1	6.1	Jun
Turkey	– 1.9	Q1	–10.4	Jun	+56.3	Jul	–20.9	Jun	– 3.7	Jun	16.6	Jun
Czech Republic	+ 3.8	Q1	+ 3.7	Jun	+ 5.9	Jul	– 3.5	Jul	– 2.7	Q1	12.9	Jul
Hungary	+ 4.4	Q1	– 0.4	Jun	+ 9.4	Jul	– 2.4	Jun	– 1.7	Jun	11.9	Jul
Poland	+ 2.3	Q1	+ 1.1	Jul	+ 5.2	Jul	–10.1	Jun	– 7.2	Jun	27.0	Jul
Russia	+ 4.9	Q1	+ 2.9	Jul	+22.2	Jul	+59.5	Jun	+45.9	Q1	31.3	Jun
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Pakistan	+ 5.6	2000†	+26.6	Mar	+ 3.6	May	– 1.5	Jul	– 1.1	2000†	1.3	May
Saudi Arabia	+ 4.5	2000§	na		– 0.2	May	+50.9	2000	+15.6	2000	17.1	Jun

*Excluding gold, except Singapore; IMF definition. †Year ending June. ‡New series § Economist Intelligence Unit estimate.

Text refers only to the first 25 countries listed

Sources: National statistics offices, central banks and stock exchanges; Thomson Financial Datastream; EIU; Reuters; Warburg Dillon Read; J.P Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Garanti Bank; Deutsche Bank; *Russian Economic Trends*.

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Financial markets

Aug 30th 2001
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Aug 29th		Dec 31st 2000	
	Aug 29th	year ago	Aug 29th	% p.a.		one week	in local currency	in $ terms
China	8.28	8.28	12.0	na	1,929.3	−3.0	−12.0	−12.0
Hong Kong	7.80	7.80	11.3	3.32	11,242.4	+0.5	−25.5	−25.5
India	47.1	45.8	68.4	6.88	3,300.6	+0.1	−16.9	−17.7
Indonesia	9,150	8,360	13,285	17.66	437.8	−0.9	+5.2	+11.2
Malaysia	3.80	3.80	5.52	3.30	689.1	+4.9	+1.4	+1.4
Philippines	51.2	45.1	74.3	10.81	1,270.6	−1.8	−15.0	−17.0
Singapore	1.75	1.72	2.54	2.23	1,634.8	+0.1	−15.2	−15.8
South Korea	1,277	1,109	1,854	4.81	565.6	−1.6	+12.1	+11.0
Taiwan	34.6	31.0	50.2	3.65	4,508.7	+0.5	−5.0	−9.0
Thailand	44.2	41.0	64.2	3.00	338.0	+5.2	+25.6	+23.3
Argentina	1.00	1.00	1.45	18.87	325.4	−0.9	−22.0	−22.1
Brazil	2.55	1.83	3.70	19.03	13,062.3	+0.8	−16.3	−35.9
Chile	656	565	952	3.90*	5,676.6	−0.2	+16.6	+2.0
Colombia	2,298	2,208	3,336	12.46	990.4	+0.7	na	na
Mexico	9.15	9.21	13.3	7.61	6,324.9	−0.1	+11.9	+17.6
Peru	3.48	3.47	5.1	5.45	1,340.8	−0.4	+11.0	+12.3
Venezuela	737	689	1,070	12.91	6,981.0	+2.0	+2.8	−2.4
Egypt	4.26	3.53	6.19	8.91	5,777.0	+3.5	−24.6	−31.2
Israel	4.25	4.01	6.17	4.42	417.0	−2.0	−15.7	−19.8
South Africa	8.33	6.96	12.1	9.67	9,034.1	+2.6	+8.5	−1.4
Turkey	1,378,000	652,050	2,000,718	63.00	9,990.2	+3.8	+5.9	−48.5
Czech Republic	37.7	39.6	54.7	5.54	370.6	+0.6	−22.5	−22.6
Hungary	278	292	403	11.00	6,348.9	−0.1	−19.1	−17.8
Poland	4.24	4.38	6.15	15.24	12,616.2	+1.1	−29.3	−31.1
Russia	29.4	27.8	42.6	25.00	207.5†	+3.8	+48.5	+44.8
EMF (MSCI)‡	1.00	1.00	1.45	na	301.9	+1.1	na	−9.6
EMBI+§	1.00	1.00	1.45	na	211.4	+2.1	na	+4.7

*Inflation adjusted. †In $ terms. ‡Emerging Markets Free. §J.P. Morgan Chase's Emerging Markets Bond Index Plus.
Sources: National statistics offices, central banks and stock exchanges; Thomson Financial Datastream; EIU; Reuters; Warburg Dillon Read; J.P Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Garanti Bank; Deutsche Bank; *Russian Economic Trends*.

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